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National Competition Policy Philosophies in the Triad: Considerations for Trade Policy

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Executive Summary

A national competition policy is a constitution for overseeing competition in the domestic market. Competition policy sets out rules and procedures for business structure and conduct in the market place. As in a constitution, however, a competition policy regime cannot possibly list a comprehensive set of rules to be followed in every conceivable instance in precise detail. In practice, competition policy is couched in terms that can be interpreted and applied as the economy and the nature of competition change in dramatic and unpredictable ways.

This Paper explores how philosophies of competition in the U.S., Japan and the EU (the Triad) have shaped the making, interpretation and enforcement of competition policy and laws in each jurisdiction. National competition philosophies, we submit, can be situated on a spectrum stretching from the individualistic to the communitarian. Why would differences in philosophies of competition policy matter in the future evolution of trade policy?

The WTO mixes elements of domestic and international economic policy rules and regulations. Competition policy analysts have cautioned that the negotiation model of reciprocal tariff reductions does not necessarily extend to the area of competition regimes. Under the WTO, there are already proposals for a search for harmonization of national competition laws. While some analysts favour quickly getting on with negotiations on the convergence of substantive national competition laws, others are sceptical whether the content of complicated agreements can at all be negotiated in the near future.[1]

The main message of this Paper is that in debating the convergence or harmonization of competition laws and their enforcement across countries, the trade and competition policy community will benefit considerably by paying attention to the basic competition philosophies that have generated existing differences in national competition laws and jurisprudence. Such an approach

[1]For example, see Jagdish N. Bhagwati and Robert E. Hudec, eds., **Fair Trade and Harmonization: Prerequisite for Free Trade?**, vols. I and II, Cambridge, MA: MIT Press, 1996.

will help sort out what competition laws and practices can or cannot be agreed upon in multilateral negotiations.

In comparing the competition policies of the U.S., the EU and Japan, this Paper argues that:

- in the U.S., the approach is economic, in search of efficiencies that emphasizes individual consumer welfare;
- in the EU, the system is political, in search of corporate and regional integration that stresses building a European community; and
- in Japan, it is legal, in search of fairness that emphasizes the welfare of the group.

The U.S. approach to competition policy places the premium on individual profit-maximizing activity and thereby achieving "efficient" market outcomes. The EU-Japanese approach promotes the development of efficient relationships by placing producers at the centre of the competition policy concerns.

Self-interest is central to individualism and is satisfied through market transactions. Under pure individualism, competitive markets are instrumental in processing information and allocating resources to minimize costs and maximize welfare.

In communitarianism, self-interested individuals use the twin institutions of the market and relationship-based networks to advance their economic and non-economic objectives. Networks of relationships can allow a communitarian society to capture beneficial spillover that may be missed by markets. Networks of relationships are guided not only by the invisible hands of market prices and sales, but also by the invisible handshakes of tacit understanding.

Competition philosophies evolve in tandem with the progress a society makes. The stage of economic development and the underlying competition philosophy in a country is likely to be central in determining the composition of its competition policy.

We document in this Paper that competition policies in the Triad countries over the last century have evolved in accordance with economic, legal and

political developments particular to each jurisdiction, which are, in turn, influenced by their underlying competition philosophy.

Recognizing, understanding and respecting the key motivations and the stage of economic development behind the differences are essential steps to avoiding conflict and towards a coordinated and globally effective competition policy.

Also critical is understanding that none of the Triad has the "best" or "ideal" competition policy. For example, the failure of the Japanese system to address adequately the lack of transparency in *keiretsu* corporate governance is serious. But the litigious and confrontational nature of the U.S. legal system (including antitrust law with treble damages, contingency fees and multiple entry points for litigation) makes many observers uneasy and arguably chills legitimate market activity.

One conclusion of this Paper is that there is no presumption that the "pre-dominant" form of competition policy in the world should be the U.S. version.

As international cooperation on competition enforcement expands and the debate on the convergence and compatibility of standards is more directly engaged, we must continue to guide ourselves by what makes sense in practice in the marketplace, and what visible, and invisible, influences may be exerted by differing "philosophies" of competition.

Résumé

Une politique nationale de la concurrence est une constitution qui régit la concurrence sur le marché intérieur. Elle énonce les règles et les méthodes relatives à la structure des entreprises et au comportement qui s'impose sur le marché. Le régime prévu par cette politique, pas plus qu'une constitution, ne peut comporter un ensemble exhaustif de règles à suivre dans toutes les circonstances et jusque dans les plus infimes détails. Dans les faits, la politique de la concurrence est rédigée en des termes qui peuvent s'interpréter et s'appliquer au gré de l'évolution parfois brusque et imprévisible de l'économie et de la nature la concurrence.

Le présent document décrit comment la conception de la concurrence aux États-Unis, au Japon et dans l'UE (la Triade) a influé sur l'élaboration, l'interprétation et l'application de la politique et des lois sur la concurrence dans chacune de ces trois entités. Selon nous, les conceptions de la concurrence que se font les divers pays peuvent se placer le long d'une échelle allant de l'individualisme au communitarisme. Pourquoi les différences de conception de la politique de la concurrence peuvent-elles être importantes dans l'évolution future de la politique commerciale?

L'OMC mélange des éléments des règles et règlements découlant de la politique économique nationale et internationale. Les analystes de la politique de la concurrence ont lancé une mise en garde : le modèle de négociation des réductions réciproques des droits ne s'applique pas nécessairement dans le domaine des régimes de concurrence. Dans le cadre de l'OMC, on a déjà formulé des propositions de recherche d'harmonisation des lois nationales sur la concurrence. Certains analystes souhaitent qu'on entame rapidement les négociations sur la convergence des lois nationales de fond sur la concurrence tandis que d'autres ne sont pas convaincus qu'on puisse, dans un avenir prochain, négocier le contenu d'accords compliqués[2].

[2] Voir par exemple Jagdish N. Bhagwati et Robert E. Hudec, éd., **Fair Trade and Harmonization: Prerequisite for Free Trade?**, vol. I et 11, Cambridge (Mass.), MIT Press, 1996.

Le principal message à retenir, dans le présent document, c'est que, dans le débat sur la convergence ou l'harmonisation des lois sur la concurrence et des modalités d'application des divers pays, les responsables de l'élaboration de la politique sur le commerce et la concurrence ont beaucoup à retirer d'une étude des conceptions fondamentales de la concurrence qui sont à l'origine des différences entre les lois sur la concurrence et la jurisprudence des divers pays. Cette démarche permettrait de départager les lois et méthodes qui peuvent donner lieu à un accord à l'issue de négociations multilatérales de celles qui ne s'y prêtent pas.

Les auteurs de ces lignes tirent de la comparaison entre les politiques de la concurrence des États-Unis, de l'Union européenne et du Japon les conclusions suivantes :

- aux États-Unis, l'approche est de nature économique : il s'agit de rechercher une plus grande efficacité, avant tout dans l'intérêt du consommateur pris individuellement;
- dans l'Union européenne, le système est plutôt politique : on recherche l'intégration des sociétés et des régions par souci de construire la communauté européenne;
- au Japon, enfin, la démarche a un caractère juridique : c'est une recherche d'équité qui met l'accent sur le bien-être du groupe.

L'approche américaine de la politique de la concurrence privilégie l'activité individuelle de maximisation du profit, ce qui se traduit par une plus grande efficacité sur le marché. L'approche de l'Union européenne et du Japon favorise le développement de relations efficaces en plaçant les producteurs au centre de la politique de la concurrence.

L'individualisme place au premier rang l'intérêt personnel, qui est servi par les transactions sur le marché. Dans un régime purement individualiste, les marchés concurrentiels permettent le traitement de l'information et l'affectation des ressources de manière à réduire les coûts au minimum et à maximiser le bien-être.

Dans le communitarisme, celui qui est guidé par son intérêt personnel a recours aux deux institutions que sont le marché et les réseaux de relations pour

atteindre ses objectifs économiques et autres. Les réseaux de relations peuvent permettre à une société communitariste de profiter des retombées bénéfiques qui peuvent avoir échappé au marché. Ces réseaux sont régis non seulement par la main invisible des prix du marché et des ventes, mais aussi par l'intervention tout aussi invisible des ententes tacites.

Les conceptions de la concurrence évoluent parallèlement au progrès accompli par la société. L'état du développement économique et la conception sous-jacente de la concurrence ont toutes les chances de jouer un rôle déterminant dans l'élaboration de la politique de concurrence.

Nous montrons dans ces pages que les politiques de concurrence des pays de la Triade ont changé, au cours des cent dernières années, en fonction du développement économique, juridique et politique propre à chacun d'eux, développement qui a subi l'influence de leur conception sous-jacente de la concurrence.

Il est essentiel de saisir, de comprendre et de respecter les motivations clés et le degré de développement économique qui expliquent les différences si l'on veut éviter les conflits et s'orienter vers une politique de la concurrence qui soit coordonnée et globalement efficace.

Il faut aussi comprendre, c'est crucial, qu'aucune des entités de la Triade n'a la « meilleure » politique de concurrence, la politique « idéale ». Ainsi, c'est une grave carence, dans le régime japonais, qu'on ne puisse s'attaquer comme il se doit au manque de transparence dans la direction des sociétés (keiretsu). Et la multiplication des litiges et des affrontements du régime juridique américain (avec une loi anti-trust prévoyant des dommages-intérêts triples, des honoraires proportionnels et des recours multiples pour intenter des poursuites), met beaucoup d'observateurs mal à l'aise et risque de freiner des activités normales sur le marché.

L'une des conclusions du présent document est qu'on ne présume pas que la forme dominante de politique de concurrence dans le monde doit être la version américaine.

1. Introduction

This Paper addresses two questions:

1. What are the philosophical underpinnings of differing national competition policies in the United States, Japan and the European Union (the Triad economies)?

2. What explains the philosophical differences among the national competition approaches in the Triad economies?

In the policy community, there is a lively debate regarding the possibility of convergence of national competition systems and about the establishment of associated international institutions. Suggestions for convergence range from "complete" convergence to "soft" harmonization.[2] Suggestions for the internationalization of competition policy range from enhanced cooperation between national competition authorities to a supra-national institution.

This Paper situates these debates from the perspective of philosophical approaches to competition. Across national jurisdictions, approaches to competition have both common elements and differences. Moreover, national competition laws may have similar wording, yet the interpretation in the case law across countries may differ or agree on substantive matters. Views toward competition are shaped by underlying but changing philosophies linked to specific social, cultural, political and economic circumstances.

Traditionally, competition policy has been viewed as the legal framework to regulate and maintain competition in a domestic market. Competition policy, as an instrument of domestic policy, can prod corporations and consumers over time to achieve efficiency and welfare-enhancing market outcomes. Consequently, competition policy can contribute to the maintenance of a well-tuned domestic economy.

[2]Under soft harmonization, national competition regimes are aligned to some internationally agreed guidelines. The language and particular details of national competition legislation may differ, but the overall thrust of the competition policy conforms to the internationally agreed guidelines. Under hard or complete harmonization, identical regimes prevail across countries.

This Paper places national competition policies along a philosophical spectrum ranging from the individualistic to the communitarian. Communitarians can allow certain cooperative or collusive business behaviour that individualists may consider restrictive of an individual's freedom in the market place. This Paper finds the U.S. at the individualistic end of the spectrum and Japan at the opposite end, while the EU is about in the middle.

The place a nation takes along this spectrum determines its choices for specific competition policy. In comparing the competition policies of the U.S., the EU and Japan, this Paper argues that:

- in the U.S., the approach is economic, in search of efficiencies that emphasize consumer welfare;
- in the EU, the system is political, in search of integration that stresses building a community out of subsidiary nations; and
- in Japan, it is legal, in search of fairness that emphasizes overall community welfare.

Trade policy has traditionally consisted of border and associated domestic measures that aim to increase the welfare of domestic and nationally-based corporations, and consumers. The rules-based trading system is directed at minimizing frictions in international commerce. The trade policy spectrum stretches from liberal and undistorted free trade to a trade restrictive approach.

In the last decade or so, the policy community has come to view the interaction of competition and trade policies as a new issue. In this Paper, we trace the trade and competition policy linkages that go back quite a bit in history. For instance, as Japan's trade policy in the 18th century shifted from a position of autarky to allow commerce with the West, the Japanese marketplace had to confront alien and aggressive U.S.-style individualistic competition. One fallout from such a liberal trade policy was that, in the late 19th and early 20th centuries, competition policy in Japan was modified to tolerate cartels among Japanese firms to face foreign competition in Japanese markets.

The Paper is organized as follows. Section 2 introduces the different philosophical approaches by focusing on the two ideal capitalist paradigms: individualism and communitarianism. Section 3 discusses competition

philosophies in a static as well as in a dynamic context. The focus is on the individualist bias in the historical development of competition policy. Sections 4, 5 and 6 discuss the development of competition philosophy in individual jurisdictions using examples from the statutes, case law and institutional arrangements. Section 7 places the Triad countries along the philosophical spectrum. Final considerations are outlined in section 8.

2. A Capitalist Philosophical Spectrum

The individual, market and society are central elements of capitalism. In capitalist economies, the philosophical spectrum stretches from individualism to communitarianism. To make a general and abstract point, individualists are focused on themselves. Communitarians have a community-based perspective that balances their rights with their responsibilities to and longer-term relationships with others. Individualists tend to compete; communitarians tend to cooperate.

The essential role of competition policy is to search for the balance between these two urges in society and in business: competition and cooperation. That is, the balance between individualism and communitarianism. The point at which this balance is struck depends on the location of each jurisdiction along the philosophical spectrum.

Individualism and communitarianism represent different visions of the role that the individual should play in the community and the role that the community should play in regulating the activities of individuals. Consequently, different shades of capitalism can emerge, depending on how different societies emphasize these roles. Over time, countries can diverge or converge on the emphasis they put on individualism or communitarianism.

2.1 Individualism

> It is not from the benevolence of the butcher, the brewer or the baker that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of our own advantages.[3]

● Self-interest

Individualism sees people free to use their peculiar knowledge and skills with the aim of furthering the objectives and interests they care for. Individualism does not mean egotism or selfish behaviour driven by one's immediate needs. Self-interest is the universal mover, which need not be limited to self-love and can include one's family, friends and society.

Individualism's main principle is that no person or group of persons should have power to decide what another person's status in society ought to be. This sense of freedom is essential to an individualist and must not be sacrificed to some other sense of justice. Individualism places the individual above the community and places self-interest above the welfare of the wider community. Nonetheless, the self-interest and limited vision of the individualist is not to be interpreted in a narrow self-centred sense. One broader view of individualism is summarized by von Hayek:

> True individualism...is primarily a theory of society, an attempt to understand the forces which determine the social life of man.... This fact should by itself be sufficient to refute the silliest of the common misunderstandings: the belief that individualism postulates...the existence of isolated or self-contained individuals, instead of starting from men whose whole nature and character is determined by their existence in society...its basic contention is...that there is no other way toward an understanding of social phenomena but through the understanding of individual actions directed toward other people and guided by their expected behaviour. [4]

Individualism contends that in cases where the coercive action of the state is usually invoked, voluntary collaboration among people would better achieve the aims. The traditions and conventions which evolve in a free society are flexible and allow spontaneous formations of groups or associations. Seemingly

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[3]Adam Smith, **The Wealth of Nations**, 1776.

[4]Frederich von Hayek, *Individualism and Economic Order*, Chicago: University of Chicago Press, 1948, p. 6.

irrational forces of society allow people to work together smoothly and efficiently with much less formal organizations and compulsion. Society is greater than the individual only in so far as it is free.

● Individualist markets

In a capitalist economy, most individualists cannot satisfy all their needs themselves and, thus, are forced to go to market. It is important to emphasize that it is their very self-interest which brings them to the market. In the process of exchanging their output for what they want to consume, individualists create markets. The fulfilment of mutual interests leads to repeated exchanges and continued market interactions among individualists over time.

To participate in the market, the individualists have to accommodate the self-interests of others. Consequently, their interactions with other individualists regulate their own actions and dilute their own self-interest. Thus, the market mechanism enables people seeking their own interest to advance the interests of all individuals in the community, a point originally popularized by Adam Smith.

● Freedom

The pursuit of individualistic freedom, in addition to self-interest, is the main drive of individualists. However, market competition can limit individualistic freedom. The contours of individualist market capitalism are shaped by the following three important freedoms:

- freedom in an impersonal market,
- freedom to choose, and
- freedom in random market order.

Freedom in an impersonal market. Competitive markets are impersonal. Through the interaction of independent individuals in a market, an individual's personality is subsumed, or offset, by those of the individuals with whom he interacts. In a competitive market, producer and consumer interests align relatively automatically. An individual leaves an imperceptible imprint in the market and market participants enjoy the freedom of anonymity.

Freedom to choose. As individualistic freedom increases with the number of participants in the market, individualistic markets thrive on new entrants. As more individualistic participants enter the market, the number of potential producers and consumers increases, which broadens an individual's freedom of choice.

Freedom in random market order. On account of the individual's limited knowledge, outcomes in competitive markets may appear to be random or accidental. The "randomness" is actually a part of the automatic realignment of the market that is beyond any individual's ken. However, it is the freedom of market participants to respond that permits them to make prompt adjustments to market changes. Consequently, the possibility of commerical exchanges provides freedom by allowing the market to re-order itself.[5]

● Information

Individualists tend to process those bits of information that they consider having a direct effect on their interests. Market prices are central to the individualistic self-interest calculus. Prices allow each individualist to evaluate quickly the worth to themselves of exchange with others. The central question is:

- Can capitalist markets costlessly supply information for short as well as long-term decisions?

If they can, then individualistic markets will be **efficient** and can achieve social optimum. However, capitalist markets in general may not do a complete job. The discipline of the competitive model can optimize aggregate income only when the acquisition of information and the bargaining among individuals are costless. Costless information and enforcement of remedies are necessary for market participants to punish deviants. However, individualists incur resource costs **and** possess incomplete information in their market dealings.

[5]Von Hayek, *op.cit.*, 1947, pp. 80-1.

Consequently, individualist decisions, as we argue below, may be based on a narrower view of society than communitarians.[6]

- **Time horizon**

Well functioning and efficient markets can provide much information that is useful to an individualistic self-interest calculation. Benefits of markets in providing information and in allocating resources in a capitalist setup are well appreciated in matters with a short-term time horizon, although in a number of instances markets do fail to perform efficiently. This argument is also valid in a model with a longer time horizon.

Individualists do consider factors that are likely to figure in their self-interest in the future. For instance, in working out the present value of future events, individualists can use discount rates based on returns in markets for longer term financial instruments, such as bonds of different maturity dates. However, it is well-known that the discount rate used by individualists often differs from the communitarian or social discount rate. For example, individualists may not adequately factor in future environmental effects not only on society but also on their own interests.[7] Consequently, individualist markets may fail to incorporate community-level considerations and a number of potentially beneficial markets may fail to emerge. In this view, individualists and their community relying on private markets alone can end up at a lower level of social welfare.

- **Individualistic corporatism**

Individualism views the firm as a legal entity which works from a commonly known production plan. Individualist managers produce products that

[6]Information acquisition is sub-optimal because individualists balance private marginal benefits and the private marginal cost of obtaining new knowledge. This individualistic calculus leaves out the community-level spillovers.

[7]In neo-classical economic theory, for the market to incorporate future developments and scarcities properly, trades in (the so-called Arrow-Debreu securities) "state-contingent claims" would have to take place for **all** the relevant goods and services to be used at future dates. Since not **all** such markets currently exist in capitalist economies, prices and sales in competitive markets cannot be taken to reflect accurately the value or importance of these goods and services.

are most likely to maximize profits or the present value of the firm.[8] Shareholders, i.e., the owners, appoint executives to act as their agents in legally contracting with outsiders (such as suppliers, dealers and financial institutions) and insiders (workers and managers).

Profit maximization, without any overlay of community considerations, underpins and motivates individualistic corporatism. The division between the profit interests of the company and the interests of its employees is well defined. Shareholders quarterly police the company profits. A short-term downturn in profits can be off-set, among other things, by the simple expedient of firing workers. Outsourcing work can also relieve individualistic corporations of both fixed costs and employee loyalty.

Capitalism thrives on the profit motive of innovations. Individualism emphasizes that innovation must be fostered by individual efforts, preferably by venture capital and gung-ho new entrants. Individualists prize the entrepreneurial flair and relish technological or business novelty for its own sake. Even managers in established corporations, knowing that the impermanence of their jobs may let them get away from the consequences of their mistakes, are eager to re-engineer, experiment and seek business adventure. Ultimately, the shareholders must see value resulting from the process of creative destruction.

Individualistic capitalists derive psychic benefits from this kind of mind-set. Individualists would trust their own judgement, rather than that of bureaucrats, to second-guess the market. Consequently, the ideal government role is limited to investing soundly in education and infrastructure. A competitive struggle among firms is preferable to run-ins with politically motivated regulations and restrictions on business.

[8]Oliver Hart, "An Economist's Perspective on the Theory of the Firm", **Columbia Law Review**, November 1989 (89): 1757-74.

2.2 Communitarianism

> How selfish soever Man may be supposed, there are evidently some principles in his nature which interest him in the fortune of others, and render their happiness necessary to him ... the greatest ruffian, the ardent violator of the laws of society, is not altogether without it.[9]

● Relationships

The key feature of communitarianism is the **relationships** among individuals themselves.[10] The glue of these social or community relationships transcends the self-interests of the individuals and binds people together. Communitarianism, however, does not deny that communities are made up of self-interested individuals. Rather, communitarianism highlights the benefits of association in addition to the fulfilment of self-interest through production and consumption activities. Market as well as non-market considerations motivate economic and social relationships among self-interested individuals. A communitarian philosophy is influenced, in addition to economic calculus, by social, cultural, political and other community level factors.

Why is it that market exchanges need be supplemented by relationships in an economy of self-interested individuals?

● Community interests

The interests of communitarians go beyond consumption, production and market exchange. Self-interested persons realize that, in the formation and development of society, the economic dimension is only one means to a higher end. People wish to realize their material and non-material aspirations. With the expanding scope of markets, people find markets convenient to achieve their objectives. However, a good many things still have to be done outside the market. In such a framework, people create arrangements that can advance their own interests by accommodating those of others. For a harmonious social order

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[9]Adam Smith, **The Theory of Moral Sentiments**, 1759.

[10]Herman Daly and Cobb, **For the Common Good: Redirecting the Economy Toward Community, the Environment and a Sustainable Future**, Boston: Beacon Press, 1989, p. 16.

and economic progress, market and non-market based exchanges are necessary among self-interested individuals.

● The time horizon

Communitarian behaviour involves self-interest, although played out over a longer time horizon. This extends the period of self-interested recoupment of the individual's production and provision beyond the horizon of the individualist. If a person provides a thing in a relationship that is not based on an immediate exchange in return, then a responsibility is created in the recipient to reciprocate to the provider later on. This sense of obligation fosters the relationship. When people hand over or get things without immediately settling accounts, the relationship building process fosters a sense of trust and a longer-term perspective. The shift from the short-term exchange to a longer-term payoff creates a strong incentive in the provider to ensure that the relationship remains strong and lasts at least long enough so that the provider is satisfied in return.

Communitarian relationships are guided not only by the invisible hands of market prices and sales, but also by the invisible handshakes of tacit understanding. Such relationships allow people to settle financial and non-financial balances over a longer period of time. What may appear to be an inefficient relationship among self-interested individuals in the short-term may actually be perfectly efficient in the long run. From the time parties begin an exchange to the time it is completed in the future, these persons keep track of each other and do things to accommodate the other party such that the final part of the exchange is performed satisfactorily. They do this because a short-term outlook conflicts with, disrupts and weakens the relationships that make up the social glue of society.[11]

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[11]Daly and Cobb, *op. cit.*, pp. 164 and 163:

> Economics based on Homo Economicus as self-interested individual commends policies that inevitably disrupt existing social relationships... the individualistic model of economic theory leads to advocating policies that weaken existing patterns of social relationships.

Winkler, *op. cit.*, p. 105:

> Alexis de Tocqueville of France...in his classic study *Democracy in America*...warned that untrammelled individualism might undermine this commitment...a connection between the individual and the larger community...to a sense of community.

What explains communitarianism?

A communitarian model

Communitarian efficiency. The process of mutual cooperation and accommodation has to be efficient. Efficiency requires that we minimize the resource expense in charting out and sustaining market and non-market relationships.[12] A successful communitarian setup meets the objectives of its members efficiently.[13] Success comes when people cooperate not only in market transactions but also cultural, political and social interactions, and not only from a short-term but also a longer perspective. An individual's self-interest motivates him to establish market and non-market links with others and become a part of the web of relationships, connections, compromises and networks in the community.[14]

The growth of networks. A number of different networks may be formed depending on social, economic and political objectives and the geographical location of the network members. Competition for success is likely to force networks to be efficient and durable and to cooperate with others in the community.[15] In such a society, there emerges an overlap of economic and non-

[12]The market and non-market point has also been argued by Ronald Coase, "The Nature of the Firm", **Economica**, 1937 (4): 386-405; Kenneth Arrow, **The Limits of Organization**, New York: Norton, 1974; and Oliver Williamson, **The Economic Institutions of Capitalism**, New York: The Fress Press, 1985.

[13]Efficiency in communitarianism is defined broadly to include economic, social, political and cultural resource costs.

[14]A network of relationships is an institution or organization made up of groups of individuals bound together by some common purpose to achieve certain objectives. Examples of such networks would include political parties, cooperatives, churches, clubs, firms. See Douglas C. North, "Economic Performance Through Time", the Alfred Nobel Memorial Prize lecture delivered in Stockholm, December 9, 1993; reprinted in **American Economic Review**, June 1994: 359-68.

[15]A network providing beneficial externalities may have to contend with the problem of free-riders. New entrants may have to demonstrate their commitment to the network by incurring some (non-economic or cultural) sunk costs, including short-term sacrifice. Outsiders to the network may interpret such practices, norms, codes of behaviour or traditions as entry barriers and protest foul play. Even the Salvation Army often requires street people to listen to a sermon before giving them free meals. See Laurence R. Iannaccone, "Sacrifice and Stigma: Reducing Free-riding in Cults, Communes and Other Collectives", **Journal of Political Economy**, April 1992 (100): 271-91.

economic interests and activities. An individual gains a community perspective and the person develops into a communitarian being—functional in the market and the community.

Institutions. Communitarians also exhibit network pluralism. A workable balance between various relationship-based networks, each pushing its view, has to be struck by intermediary institutions. For this purpose, society develops common practices, traditions, conventions and other cultural institutions in a market setting.[16] The non-market communitarian arrangements are helped by features such as:

- **Transparency and fairness.** For the stability of the relationships in the model, the members of society have to be comfortable about the fairness of a decision in the community, even if they do not particularly like it.

- **Mutual accommodation.** The network system has to reconcile the differences in preferences of wealth-maximizing individuals. Individuals can rely on long-term relationships for the payoff to offset any perception that a particular individual or network is being challenged or subjected to a narrow-minded imposition by others in the community.

For example, a decision in the long-term interests of the community may impose short-term restrictions on individual or group behaviour and choices. Such a decision can be made acceptable provided people become convinced that the decision does not unfairly give an advantage to someone else's group. As a result, the process of economic, political and social decision-making entails a discussion of community interests and trade-offs, and consensus building. Such a process also fosters a sense of civic responsibility, and helps along the enforcement of decisions and the resolution of disputes.

[16]Douglas C. North, "Institutions", **Journal of Economic Perspectives**, Winter 1991 (5), 97-112: Institutions are the humanly devised constraints that structure political, economic and social interaction. They consist of both informal constraints (sanctions, taboos, customs, traditions and codes of conduct) and formal rules (constitutions, laws, property rights).

● Relationships and markets in communitarianism

Communitarians do produce in order to participate in market exchange and so receive something in return that will satisfy their needs. Above we described the short-term character of market relationships. Communitarians would use market transactions provided they minimize the resource cost **and** are consistent with other efficient arrangements and accommodations in the community. In this view, there emerges a tug between efficient markets and efficient communitarian relationships. Depending on the relative efficiency merits[17] of markets and relationships, we can derive the following predictions from this model:

Proposition 1. In general, there will co-exist transactions that go through the markets as well as those done on the basis of relationships and also those that are mixed.

Proposition 2. Transactions that markets do not process efficiently will go through the network of relationships.

Proposition 3. Where using the relationship network entails hefty resource costs, transactions will be done in the marketplace.

● Information

If we could develop relationships quickly, the resource expense would be small. However, relationships are based on knowledge. We need information about economic and non-economic factors in the short and long-term. To sort out what is relevant, in addition to this information our judgement is essential. Relationships can be helpful in the formation of our judgement about things. What are the sources of knowledge for decision-making in a communitarian setup? In addition to market price information, these sources are common practices, shared ways of doing things, customs, traditions and other cultural and social institutions. Efficient traditions and commonly shared practices and attitudes emerge whenever other mechanisms, such as the market system, appear to perform less satisfactorily and inefficiently.

[17]Recall that efficiency includes resource costs such as economic, social, political and cultural efforts.

- **Freedom**

Just as the combined force of interaction among self-interested individualists dilutes any one party's influence, so too does community-interest under communitarianism dilute the more individualistic elements of exchange. Some communitarians more readily subsume their self-interest in exchange for the benefit of the relationship itself.

- **The inclusion of market failures**

Communitarian thinking not only allows more comprehensive (economic and non-economic) consideration of community-level static effects of a person's decisions, but also consequences that emerge over time. In this view, markets based on narrow and short-term individualistic thinking are ahistorical. In contrast, the community learns from the experiences of its members, develops its own memory and has its own history. These properties enable communitarians to better take account of society-level externalities and include the spillovers in decisions made in the community.

- **The use of the legal system**

Cultural factors affect a society's approach to conducting itself. An individualistic society of equals has a stronger need for the imposition of an external order. A communitarian society already contains an internally self-imposed hierarchy based on relationships. On the legal front of private governance, formal contracts are less necessary in a communitarian system for three reasons.

- First, the process of getting to know one another is so long and convoluted that the relationship is especially strong, and exerts an independent force which is more flexible, durable and reliable than a contract.
- Second, by the time an agreement is reached between two parties, a relationship already exists.
- Third, the reliability of the relationship is in its flexibility; the reliability of a paper contract is in its rigidity, fixed by its legal remedies for breach.

Remedies are sought through informal negotiation relying on the relationship itself, rather than on the formal rights on paper. Litigation is even less an option because its adversarial nature endangers the underlying relationship. More so than contracts, law suits level hierarchy by placing parties on a scale, equal to each other before the law. Furthermore, going to court means breaking off the relationship and subjecting it to an external review, admission of a failed relationship.

The presence of legal remedial power adds the extra chill of subjecting the relationship to an external review that is, in the communitarian view, unnecessary and even threatening to the relationship itself. Such external review is anathema to the relationship so arduously cultivated. Thus, a communitarian society prefers informal but "real" agreements between people over formal and "artificial" constructs on paper. Resorting to formal constructs to build and govern relationships, or to remedy violations is not as necessary. Formal controls are required only as a last resort.

- **Communitarian corporatism**

In a communitarian setup, corporations must survive in the long-run. Corporate stability is prized not only by the business and shareholders but also by workers. One way to achieve long-term survival is to focus on growth in the company's market share and, if necessary, to strike a trade-off in favour of lower short-term profits, or even low profit levels over many years. On the strength of trust in the relationship between managers, shareholders and workers, communitarian corporatism develops a long-term view of corporate profits.

Under communitarianism, one corporation is connected with others in a web of vertical and horizontal business relationships. A firm is most likely to be a member of a relationship-based communitarian network. Corporate links could extend across several networks depending on what route is efficient for commercial success. Corporations have backward linkages to resource and input suppliers, and forward linkages to distributors and consumers in the final market. The corporation conducts its business by incurring communitarian obligations to some corporations and by extending communitarian credits to others. In time, accounts receivables are realized and outstanding accounts are settled.

Communitarian firms realize that they have to be competitive on world markets to ensure that they continue to benefit from the stable and cooperative arrangements, practices and institutions in society. Corporate financial success must translate into prosperity for the community: for the shareholders, for the workers, for the government and for the consumers. Mutual loyalty and trust between the corporation and employees can go a long way in keeping production costs and product quality high. More importantly, firms prize their human resources and value effective co-operation with other firms in the community. Workers are fired, not as the first option, but as a last resort. Not only do firm-employee relationships tend to be durable, firm-to-firm relationships, especially within one's own network, tend to last too.

3. Competition Philosophy

3.1 The basis of individualistic competition philosophy

Recall that self-interest and individualistic freedom shape the contours of individualistic market capitalism. An individualistic market economy can enhance individualistic freedom and self-interest as the number of rivals increases. Where the number of rivals decreases, so too do the freedoms. Restoring the freedoms in the market is the essence of individualistic competition policy.

- **Fairness**

The market mechanism is eminently self-regulating. The medium of flexible prices is central to this function. Despite the different perspectives individuals bring to market, in the individualist world-view exchange ideally takes place between equals. Depending on demand and supply conditions, individualists may earn unequal amounts for what they trade. Yet their relationships remain equal so long as they are voluntary and free. Competitive market relationships are acceptable to individualists if they believe that the exchange is fair and between relative equals.

- **Individualistic collusion**

The freedoms of the market are of benefit to all individual participants. However, if an individual can subvert the freedoms by acquiring control over the market, increasing his information relative to his counterparts or by limiting their options, then he can extract larger profits. In the abstract model where transactions are costless, the bargaining strength of an individual does not affect the efficiency of markets. But in a world of positive transactions costs, individuals can achieve a quietly dominant position.

Whenever one party becomes dominant in the exchange, the relationship becomes unequal. Individualists facing the dominant market players may feel a reduction in both their choice of trading partners and in the voluntariness of their participation in the exchange.

- **Unfair market dominance**

Dominant market players seek to impose their personality over the impersonality of the market. Monopoly prices destroy the immaculate amorality of the market order. In markets where monopoly or oligopolistic exploitation is possible, however, the consideration of equitable prices or wages becomes relevant.[18] Dominant players seek to reduce the options of others, by making themselves the only option.

Dominant players apply their own order to market disorder and uncertainties. It is one thing to accept one's helplessness before disorder; it is unacceptable, especially for an individualist, to be helpless before the order of another. We can accept accidental misallocations, but we cannot accept misallocation by coercion. As monopoly order enters a market, its fairness has to be examined. It is unfair for a participant to be independent from market forces, and it is unfair for other participants to be made dependent upon that dominant player.

[18]Von Hayek, *op.cit.*, 1947, p. 111:
What standards we have are derived from the competitive regime we have known and would disappear soon after the disappearance of competition. What we mean by a just price, or a fair wage is...the price or wage that would exist if there were no monopolistic exploitation.

Limiting freedoms

The strength of the individualist's self-interest and individual freedom militates against such dominance and its coercive effect. If individualists cannot prevent such monopolization or dominance, they may demand a protection external to them as individuals. Thus, individualists accept some governmental regulation because it can represent, like the market, their aggregate interests, and help ensure that the market remains free from unacceptable control by a few players.

Such governmental regulation is developed in an eminently individualistic way. Individualistic communities contain relative strangers. To facilitate communication or resolve disputes, it is necessary to impose some agreed order. Where the individualistic society lacked a natural commonality of understanding, stemming from longer-term relationships, it created one that could be understood by all: the order of logic. In Western societies, that order was found in law, based on a tradition from the logical thinking of Greek philosophy and logically structured languages.

3.2 Motivations of individualistic competition law and policy

> The legislature, were it possible that its deliberations could be always directed, not by the clamorous importunity of partial interests, but by an extensive view of the general good, ought upon this very account, perhaps, to be particularly careful neither to establish any new monopolies of this kind, nor to extend further those which are already established. Every such regulation introduces some degree of real disorder into the constitution of the state, which it will be difficult afterwards to cure without occasioning another disorder.
>
> Adam Smith[19]

Due to the tension, natural in an individualist market, between the freedom of the market and the private interest in subverting the market, a need develops for an external control in the form of competition law and policy. Competition policy serves three masters, each in a way that emphasizes the concerns of individualism.

[19]Adam Smith, ***The Wealth of Nations***, Book IV, Chapter 11, 1776.

- **Competition policy protects economic freedoms**

Competition policy is economically motivated: it protects the efficacy of the market by seeking an efficient allocation of resources. When we ask:

> What is the core of antitrust?.... Antitrust is economic freedom...without antitrust the free market would not long be free.[20]

Competition policy is an individualistic form of organization because it is essential to regulate a market of self-interested individuals.

- **Competition policy protects legal freedoms**

Competition policy is also legally motivated: it protects the rights of market participants.

While competition policy is one of the laws most linked to economics,[21] it is not a programme of economic planning but a system of rights and remedies enforced primarily through litigation in the courts.[22] Even in this

> ...efficiency-oriented area of the law, judges must make choices that they cannot derive from economics alone...economics is rarely dispositive of the legal issues.[23]

Being law, and largely judge-made law, antitrust draws on the values eminent in the common law tradition in countries such as the U.K. and the U.S.,[24] the most important of which is equity. Since the time of Solomon, equity has been

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[20]Eleanor M. Fox, "Antitrust, Trade and the Twenty First Century: Rounding the Circle", **The Handler Lecture**, New York, May 26, 1993, p. 53 (citing Cardozo, p. 1306).

[21]Eleanor M. Fox, "The Politics of Law and Economics in Judicial Decision Making: Antitrust as a Window", **New York University Law Review**, (61) 1986, 559.

[22]L.A. Sullivan, "Economics and more humanistic disciplines: what are the sources of wisdom for antitrust?", 125 **University of Pensylvania Law Review**, 1227.

[23]Fox, *op.cit.*, 1993, p. 554.

[24]Sullivan, *op.cit.*, 1241.

concerned with fair distribution.[25] The law's essence is in resolving disputes based on rights; this focus reveals its individualistic bent.

- **Competition policy protects political freedoms**

Competition policy is also politically motivated: it protects the democratic right to be free from control.

In controlling dominance and ensuring that markets remain competitive, competition policy has political benefits. Competitive markets are a corollary of democracy.[26] Dominance in a market skews the dispersal of power and control in society. Indeed, democracy is practically meaningless if economic power is concentrated in the hands of a few individuals or firms.[27]

This is an eminently individualistic view. The desire for freedom from control, or the desire that control be limited to institutions which the individual understands and can participate in, represents the political underpinning of

[25]Sullivan, *op.cit.*, 199, pp. 1240-1:

> In choosing among alternative antitrust rules, effects on goals like economic efficiency and such social amenities as wider ranges of opportunity or choice for individuals would be of interest, but the ultimate goal of analysis might be to identify not the rule most conducive to such maximization of these values, but the rule most consistent with their just distribution.... It may not be enough to ask which rule yields the greatest efficiency or even which rule maximizes individual opportunity. It may be necessary, in addition, to ask who is benefited, and in what degree and to consider the justice of that distribution.

[26]Jorde and Teece, "Introduction", in **Antitrust, Innovation and Competitiveness**, Oxford University Press, 1992, p. 5:

> Open and competitive systems are...often seen as a corollary of democracy. Indeed, in part, it was concern about the political power of the trusts that motivated the passage of the Sherman Act in the first place.

[27]McGowan, "Competition Policy in the European Union: A 1990s Perspective", a paper presented to the conference on National Competition Policy Institutions in a Global Market, Ottawa, 1994, p. 4.

antitrust.[28] Antitrust has been described as a vital component of American culture, for example, desirable for its own sake like political liberty.[29]

Freedom from control also includes freedom from government control. While individualist competition policy involves market intervention, the emphasis is still on the market. In this view, competition policy represents a more limited type of government control, a form that is less interventionist than direct regulation.

3.3 The basis of communitarian competition philosophy

> In civilised society, man stands at all times in need of the co-operation and assistance of great multitudes, while his whole life is scarce sufficient to gain the friendship of a few persons.[30]

Communitarians establish extensive networks to search out beneficial market and non-market relationships. However, we need to ask:

- Under what circumstances and at what point can the performance of the relationship-based networks be undermined by dominant groups in a communitarian setup?

Once the efficient relationship-based networks come to serve narrow group interests, the domination of the networks will not only impose economic costs but also undermine the common good in the community.

Dominance can emerge in a communitarian society. The difference, though, is that the motive to create the dominance is group-interest. In a communitarian setup, in joining a network of relationships an individual lowers

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[28]Sullivan, *op.cit.*, 199, p. 1223:
The political consensus that supports antitrust comes from other sources. Americans continue to value institutions the scale and workings of which they can comprehend. Many continue to value the decentralization of decision-making power and responsibility.

[29]Frazer, **Monopoly, Competition and the Law: The Regulation of Business Activity in Britain, Europe and America**, Sussex: Wheatsheaf, 1988, p. 3; citing Rowe, "Commentary: Antitrust as Ideology" 50 **Antitrust Law Journal** (721), 1981.

[30]Adam Smith, **The Theory of Moral Sentiments**, 1759.

the need for the recognition of self-interest rights, since those are off-set by the benefits derived from the network. Network relationships need not be based on equality. Hierarchical structures are thus more accepted in a communitarian society. This creates less of a concern with dominance itself, so long as the dominance does not lead to "unfair" extractions.

● Communitarian top dogs

A well-functioning communitarian system would permit individuals and firms to join or exit relationship-based networks. Entry and exit is likely to be a protracted process. An efficient network would have some critical membership mass. A progressive communitarian society would experience the demise of old, inefficient networks and the formation of new relationship-based networks to respond to changed circumstances. A successful network would be able to adapt to the requirements of its members and flourish in the long-term. In general, we would expect communitarianism to exhibit competition among networks based on relationships. However, networks can subvert common good and freedom in a communitarian society. Consider the following examples.

First, it is possible that relationships themselves may grow to such a strength that they prevent other relationships from forming with them. As this would militate against the continued growth of the community, a communitarian society will punish excessive dominance only so far as it threatens fundamentally to weaken society's capacity to develop relationships.

Second, in its pursuit for growth a network may carve out a dominant position for its group in the community. As long as the dominant group is open to new members and does not abuse its position in the community and market, the dominant group does not impede the efficiency, harmony and progress in the community. However, if one dominant group uses its position to gain unfair advantage over people and firms in other smaller networks, it will adversely affect community welfare.

Third, some networks could combine themselves in a cartel-like arrangement vis-à-vis others in the community. Consequently, social welfare of companies and individuals outside the cartels would be adversely affected. In such a situation, it would become important that the freedom of adversely

affected parties be restored by controlling the group behaviour of the cartelized networks in the community.

In general, networks based on relationships can be efficient and beneficial to the community but it is also possible that these networks can adopt policies that would negatively affect outsiders and rob them their rightful opportunities and freedom. Thus, there emerges a role for the formulation and enforcement of competition policy in a communitarian system.

When it comes to controlling the dominant behaviour of one group, communitarian societies require less of an imposition of an external order. The relationships among members of a community are characterized by a greater understanding of each other and each other's position. There is less need for an external order, such as logic, law or legal courts, to assist them to understand each other, or to compel them to follow a common framework. There is, consequently, less emphasis on the order found in law.

3.4 Communitarianism vs. individualism

● Interests

While individualists focus on their own needs, communitarians focus on balancing their needs with those of others with whom they have a longer-term relationship. While individualists focus on their own rights, communitarians focus on balancing their rights with their responsibilities to others.[31] Individualists are motivated by short-term self-interest in production and consumption. Communitarians are motivated by a long-term, community-interest in production and consumption. To this end, communitarians build relationships between each other.

● Market and non-market relationships and networks

[31]Kenneth Winkler, "Communitarianism" **Utne Reader**, (111) 1994, p. 105:
...communitarianism is a movement based on an effort to balance individual rights with community responsibilities.

Individualists rely primarily on market exchanges. Each market transaction begins anew. Where individualists cannot write enforceable contracts, individuals see no favourable trade-off for sacrificing something today in the expectation of a payoff in the future. In contrast, communitarians would supplement market transactions with non-market exchanges based on longer-term economic and non-economic relationships. Communitarians use the institutions of the network in the game of maximizing their wealth. They usually find it worthwhile to cooperate with other players because the game is repeated over time. Networks of small numbers of players develop to enable communitarians to find out information about the other players' past performance. The individualists turn the game upside down. For them, cooperation is difficult to sustain when the game (transactions) is not repeated, when information on the other players is lacking and when there are large numbers of players.[32]

- **Market and network time-horizons and spillovers**

Economy-wide spillovers are important in both static thinking and the longer-time horizon framework. If market prices and sales fail to incorporate these spillovers, the individualists' view can turn out to be narrower than the community-wide perspective.[33]

In short, to individualists the market mechanism is the most attractive forum to fulfil their short and long-term objectives. Since markets may either settle at suboptimal terms (i.e., prices) or fail to emerge altogether (especially where substantial spillover effects exist), market-based options are reduced and individualists are likely to miss out on a number of welfare enhancing transactions. Where markets fail, communitarians rely on relationships. Even in the presence of spillovers, communitarian transactions can take place, such that social welfare can be higher than under individualism.

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[32]Douglas C. North, *op.cit.*, 1991, p. 97.

[33]We are comparing the scope of individualist thinking with a communitarian perspective in the private sector that incorporates society or economy-wide spillovers or externalities. We submit that communitarians can undertake this incorporation more comprehensively and economically than individualists. This hypothesis, however, is not the same as seeking to supplant market outcomes with government intervention. The usual policy debate on this latter issue turns on whether bureaucrats can outperform markets. We strongly agree with neoclassical theorists that, in general, market outcomes are to be preferred over government intervention. But that is another debate.

In a communitarian set-up, political and economic institutions determine economic performance. Over time, individuals learn about the opportunities the institutional matrix provides and shape the way institutions evolve. Cumulative beliefs, norms of behaviour, conventions, self-imposed codes of conduct embodied in individuals and groups are passed on intergenerationally by the culture of a society. Competition among institutions, reflecting scarcity, induces networks to survive by learning and adapting to change. However, the greater the degree of monopoly power in an institution, the lower is the incentive to learn and adapt.[34]

- **Freedom and dispute settlement**

The direct scope for a person's freedom is much wider in an individualistic economy than under communitarianism. Individualists strike out aggressively on their own, bend and break the conventional ways of conducting affairs, and challenge established norms and habits. Individualists are equally willing to face the adverse results of their experimentations. Individualists are always on the go and their society is in flux. The cost of missed opportunities on account of market failures is not a concern for the individualist; people hit by those costs fall by the wayside. Individualists are combative, strident and aggressive in seeking the resolution of disputes and are quick to resort to courts on to pursue their "rights" before administrative tribunals or proceedings..

In contrast, communitarians value conventions, traditions and commonly agreed ways of doing things, and seek consensus in a socially and economically interdependent community. They do not find it insulting to fall in line with others and long-established practices;[35] they see efficiency in such practices. They see their behaviour consistent with the maintenance of social cohesion and harmony. Communitarians prize continuity. Thus, dispute resolution is first attempted through informal means in the community before the communitarians formally turn to courts. In many situations, the settling of differences can be speedy, economical and efficient through long-trusted relationship-based

[34]Douglas North, *op. cit.*, Nobel Laureate lecture, 1994.

[35]For a discussion of conformist group behaviour, see Robert J. Shiller, "Conversation, Information and Herd Behaviour", **American Economic Review**, May 1995 (85): 181-5.

networks. On the other hand, the use of courts and lawyers may entail hefty costs.

- **Corporate governance**

The longer-term profit horizon under communitarianism requires that firms ensure their survival well into the future. Higher short-term profits are sacrificed in favour of corporate survival. In contrast, under individualism the company is a black-box that stands apart from, and may not perceive any obligation to, the community.

The shorter-term and narrower outlook of the individualist can lead to a focus on profit maximization over a shorter period. Shareholders under individualism stress performance evaluation on a quarterly basis. In contrast, corporate managers may accept, at best, a trade-off between lower profits in the next couple of quarters against higher profits in the future on the basis of more complex circumstances and/or technical information that are not well appreciated by the stock market.[36] Such a project would have a higher chance of getting approval under communitarian thinking than under individualism.[37]

3.5 The evolution of competition philosophies

Competition policy regimes adjust to changes coming from factors such as economic, social, political and religious thinking. Although both Europe and Japan share a history of partly using individualistic competition philosophy, they have developed national competition regimes to suit their markets and society.

In the U.S., as we argue in section 4, competition policy evolved from the objective of equity protection to efficiency promotion, but retained its individualistic bias throughout. In Europe, the individualist ethic had to give

[36]For theoretical comments on corporate income smoothing in a longer time horizon model, see Drew Fudenberg and Jean Tirole, "A Theory of Income and Dividend Smoothing Based on Incumbency Rents", **Journal of Political Economy**, February 1995 (103): 75-93.

[37]This is not to say, however, that corporations under communitarianism normally outperform those under individualism. Different philosophical approaches have an impact on corporate strategies; they do not guarantee results in practice. Judging results is entirely an empirical matter.

way to the political "Community" requirements of integration. In Japan, competition philosophy started out on a base of communitarian thinking and has retained that orientation despite foreign (individualistic) competition policy influences.

The evolution of corporate management has also contributed to cross-pollination of business practices among countries. For example, Japanese firms took over the mass production techniques of U.S. manufacturers and added such profitable dimensions as quality, reliability and the provision of different products for different segments of the market. In the 1980s, U.S. industry felt a loss of manufacturing competitiveness and looked at the Japanese practices. Subsequently, U.S. companies discovered their own version of the Japanese art of *keizen*, or continuous quality improvement, "just-in-time" delivery of parts and lean production.[38] Even within the EU, cross-border mergers and acquisitions have been instrumental in the cross-pollination of business and management practices.

In section 4, we examine the way in which a "structuralist" competition policy naturally develops in an individualist market. A structural approach to competition policy focusses on breaking up dominant groups and decentralizing power. As it attempts to increase the number of rivals in the market, it is most suited to an individualistic regime.

4. United States of America

When the antitrust movement arose in the U.S., the basic structure of its society was set. Being made up of immigrants from many countries, it was a most heterogeneous market. It was already integrated on two levels.

First, the new experiment in democracy melted away many of the differences between the incoming cultures. The freedom of movement, that immigrants had already experienced in coming to the U.S., was reinforced as people moved further West, opening up new lands and applying their skills to exploit new opportunities.

[38]**The Economist**, "A Survey of American Business: Back on Top?", September 16, 1995, pp.5-6.

Second, the market in the U.S. was becoming physically integrated as the railroads linked the country. In this sense, the U.S. was the first *common market* of a continental scale, allowing freedom to trade across state lines. Trade flourished.

4.1 From fairness to structuralist efficiency

4.1.1 The individualist frontier

As people moved westward in the U.S., there was an atmosphere of frontierism. Both the railroaders and the people they served were self-interested individualists. The process of deeper market integration across the U.S. states helped the economy become more self-sufficient and independent from England and the rest of the world.

- **Trusts: the erosion of equity and freedom**

The railroad owners created monopolies and strengthened their market power through predatory pricing. Businesses formed trusts to drive out their rivals and to increase their profits. As small businesses and farmers lost out to trusts, the distribution of income in the U.S. tilted in favour of big business. Equity issues surfaced and the related policy questions became sharper.

- First, responding to the populist reaction, the U.S. government in the 1880s passed the Interstate Commerce Commission Act, which was aimed to prevent the railroads from using their monopoly power.
- Second, having put the boots to the railroads, the U.S. government's next significant act was the passage of the antitrust laws.

- **Antitrust: restoring equity**

Antitrust laws were demanded by the dominant frontier mentality in the U.S.. Small landowners argued that the trusts had hiked industrial prices relative to farm prices. Bork states that:

antitrust...is in the good old American tradition of the sheriff of a frontier town.[39]

The laws that resulted epitomized the frontier ethic, in terms of for whom, against whom and how justice was meted.

Moreover, when the Sherman Act was passed in 1890, about 40% of the U.S. workforce was engaged in farming. The antitrust legislation in the U.S. was as much a child of the prairie frontier as in other prairie countries such as Canada, which adopted its competition policy in 1889, and Australia, which enacted antitrust laws in 1906.[40]

Broadly speaking, the development of U.S. antitrust laws and enforcement may be summarized by the following characteristics:

- the protection of small business,
- trust busting,
- the preservation of economic freedom, and
- the break-up of large firms.

a. For whom the bell tolls: small business

The many voices calling for protection produced an antitrust law that has been identified as protecting a number of interests.[41] The abuse in question was the trusts' search for profits and power that sought the subversion of the market, and the imposition of the self-interest of the trusts over others. The drafters of

[39]R. Bork, **The Antitrust Paradox: A Policy at War with Itself**, New York: Basic Books, 1978, p. 6.

[40]F. Scherer, **Competition Policies for an Integrated World Economy**, Washington: The Brookings Institution, 1994, p. 17.

[41]See R. Bork, **The Antitrust Paradox**, *supra*, and Blake and Jones, "Toward a Three Dimensional Antitrust Policy", 65 **Columbia Law Review** 422, 1965; F.M. Scherer, **Competition Policies for an Integrated World Economy**, Washington: The Brookings Institution, 1994; K.G. Elzinga, "The Goals of Antitrust: Other than Competition and Efficiency, What Else Counts?", 125 **University of Pensylivania Law Review,** 1191; Lande, "Chicago's False Foundation: Wealth Transfers (Not just Efficiency) Should Guide Antitrust", 58 **Antitrust Law Journal**, 631; L.A. Sullivan, "Economics and More Humanistic Disciplines: What are the sources of wisdom for antitrust?", 125 **University of Pensylivania Law Review,** 1214; and Timberg, "European and American Antitrust laws: A Comparison", **Antitrust Bulletin** (131) 1962.

antitrust legislation in the U.S. recognized that the public's sentiments lay with small business.

b. It tolls for thee: trusts

Small businessmen thought they had rid themselves of the last of oppression at the Boston Tea Party. Instead, they found that the oppressive tithes and tea taxes of the colonial government had been replaced by monopoly prices. Consequently, the Sherman Act reflected the economic application of the U.S. founding fathers' dislike of oppressive government power. Antitrust enforcers were trying to substitute control by the invisible hand of the competitively structured marketplace for the visible fist of corporate giants operating as private governments.

c. It tolls for liberty...

The Sherman Act was designed to be a charter of economic liberty.[42] The vast profits of monopoly trusts and their large size enabled them huge power over the marketplace. Such power allowed them independence from market discipline so they could exert their own discipline over their rivals and customers. The U.S. Sherman Act aimed both at agreements that restrain trade, and create trusts and dominant positions, and at the power they exerted.

The solution to such independent power was to break up the anticompetitive agreements and dominant positions and to allow the market interactions of rivals, especially small business rivals, to reassert their freedom to operate.

For example, Section 1 of the Sherman Act prohibits agreements or understandings, express or implied, between two or more persons or firms that restrain trade in any product or service. Section 1 focusses its *per se*

[42]Rahl, "Competition and Antitrust in the United States and the EEC", 7 **Common Market Law Review,** (205) 1970, p. 294 (citing *Northern Pacific Railway Co. v. U.S.* 356 U.S. 1, (4) 1958, p. 4).

prohibitions[43] on agreements, or relationships, which create the trust. Moreover, Section 3 of the Clayton Act makes it unlawful to enter into agreements with respect to goods, wares, merchandise, machinery, supplies or other commodities, which can be characterized either as tying agreements, exclusive dealing agreements, or total requirement agreements, if the effect of such agreements may be to lessen competition substantially.[44] Furthermore, Section 5 of the Federal Trade Commission Act prohibits all unfair methods of competition and unfair or deceptive acts or practices.[45]

Section 2 of the Sherman Act prohibits any firm, acting alone or with another, from illegally monopolizing or attempting to gain a monopoly over a particular product or service. Section 2 cuts right to the heart of the concerns of small business, by focusing, in its first element, on power.

Antitrust was supposed to work for the good of all participants, including monopolists blinded by their self-interest. Their size was not only bad for their smaller rivals, but bad for themselves. By removing themselves from the discipline of the market, corporate giants were reversing the Darwinist natural selection process of the market order such that the plodders and fattest survived in the place of the fastest and fittest.

d. The tolling: the structuralist cases

In the true frontier spirit, the antitrust sheriff did not sift evidence or distinguish between suspects and solve crimes, but merely walked the main street and every so often pistol-whipped a few people, especially the very big

[43]Under a *per se* rule, it is only necessary for the complainant to prove that certain conduct occurred and that it fell within the class of practices "so plainly anti-competitive" that they are subject to *per se* prohibition. Once a court finds that a standard of *per se* liability applies, no further proof of anti-competitive effects is required. According to the *rule of reason* approach, in contrast, the plaintiff/applicant must show that the impugned practice has had an adverse impact on competition.

[44]On such vertical restraints, see I. Prakash Sharma, Prue Thomson and Keith H. Christie, "Delivering the Goods: Manufacturer-Retailer Relations and The Implications for Competition and Trade Policies", **Policy Staff Paper** No. 94/11, Ottawa: Department of Foreign Affairs and International Trade, December 1994.

[45]Sherman Act, 15 U.S.C. § 1; Clayton Act, 15 U.S.C. § 14; and Federal Trade Commission Act, 15 U.S.C. § 45.

ones. One of the very first antitrust cases, involving the railroads, made it clear that the structural approach would be *per se* and powerful.[46]

When the U.S. Supreme Court ruled in 1911 that Standard Oil had violated the Sherman Act and must be broken into thirty-four separate companies, it became clear that Congress had created a powerful antimonopoly weapon. Subsequently, major structural breakups were ordered by the U.S. courts against American Tobacco (1911), du Pont (1912), the Pullman Company (1944), the five leading motion picture producers (1940s) and American Telephone and Telegraph (1982).

4.2 From efficiency to anti-structuralism

4.2.1 Judicial balancing

While the antitrust sheriff went on the warpath against the trusts, the U.S. courts sought to shift the U.S. government away from its focus on bigness to provide some consideration of the benefits of bigness, and also to limit the power of antitrust enforcers.

In 1911, at the height of the deconcentration programme, the U.S. Supreme Court in *American Tobacco* admitted that it was not concerned with "every" contract in restraint of trade, but only those contracts that restrained trade "unduly".[47] An examination of undueness necessarily involves an examination of the effects of a measure. Considering effects adds other factors to the mix than relying purely on whether an activity falls within the narrow confines of a prohibition.

The economics of the Chicago School of antitrust was founded on such an individualistic philosophy. Chicagoans argued that the goal of antitrust is not small business welfare and the control of power, but consumer welfare, as reflected in prices.

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[46]R. Bork, *op.cit.*, 1965, p. 6.

[47]*U.S. v. American Tobacco*, 221 U.S. 106, 179, 1911.

> The maximization of economic surplus, which is the sum of consumers' surplus and producers' surplus, is conventionally stated as the goal of Chicago School antitrust policy.[48]

4.2.2 The Chicago School

Chicagoans noted the equity-based goals that antitrust was trying to achieve, but proposed that the pursuit of efficiency itself would best achieve these goals.

Rather than directly confronting equity issues such as power, the Chicago School directly looked at prices. Rather than zero in on the struggle between small business and large, the Chicago School tightened the focus to the struggle between producers and consumers. Producers are concerned with one thing: profits. Consumers are concerned with one thing: prices. Producers want prices to go up; consumers want them to go down.

Efficiency was seen as a means towards reaching other ideals too, such as freedom of choice and the equitable distribution of resources. Inefficient arrangements were also inequitable. Consequently, a direct attack on inefficiency would promote equity.

> Efficiency is not an ultimate goal. It is an intermediate goal pursued in order to facilitate freedom of choice, to serve other interests of consumers and to make the best use of society's resources.[49]

> In sum, the pursuit of efficiency goals through antitrust enforcement is consistent with the objective of equitable distribution of income...Equity goals...are indirectly and costlessly promoted by a direct attack on inefficient, anti-competitive market structures and practices.[50]

The Chicago School argued that the interaction of competitors in the marketplace would lead to efficient outcomes. Market forces help achieve allocative efficiency and lead to distributional equity. Bigness and inter-corporate arrangements should be viewed through the lens of efficiency. This

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[48]Hovenkamp, "Chicago and its Alternatives", **Duke Law Journal** (1986), 1018.

[49]E.M. Fox, "The Modernization of Antitrust: A New Equilibrium", 66 **Cornell Law Review** (1981), 1180.

[50]K.G. Elzinga, "The Goals of Antitrust: Other than Competition and Efficiency, What Else Counts?", 125, **University of Pensylvania Law Review**, 1195 and 1202.

militates towards reduced government intervention, including antitrust actions, although not none at all.

4.2.3 Chicago and the courts

One example of the active use of the populist *per se* rule was the 1967 *Schwinn* case, in which the U.S. Supreme Court condemned as *per se* violations of the Sherman Act the territorial marketing and other restrictions imposed by the Schwinn bicycle company upon its distributors.[51]

The first example of the New Learning promoted by the Chicago School came just ten years later, in the 1977 decision of the U.S. Supreme Court in *Sylvania*,[52] which reversed the *Schwinn per se* rule and relied expressly on the writings of Chicago School commentators.[53] It postulated a **rule of reason** which stated that:

> the fact finder weighs **all of the circumstances** of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition.[54]

Once efficiency had established its beachhead amongst the factors to be considered, it sought to expand its role. In this and subsequent cases, economic values are accorded predominant if not exclusive weight as compared with social and political values. The efficiencies of vertical and territorial restraints imposed by a dominant supplier upon its distributors can outweigh other concerns.

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[51] *U.S. v. Arnold, Schwinn & Co. et al*, 388 U.S. 365, 1967.

[52] *Continental T.V., Inc. et al., v. GTE Sylvania Inc.*, 433 U.S. 36, 58, 59, 1977.

[53] Barry Hawk, "The American (Antitrust) Revolution: Lessons for the EEC?", 1988, **European Competion Law Review** 53, 60; see also Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585, 1985; Fishman v. Estate of Wirtz, 807 F. 2d. 742 (7th Cir.), 1986.

[54] Schechter, "The Rule of Reason in European Competition Law", **Legal Issues of European Integration**, p. 7, citing *Sylvania*, p. 49.

● The primacy of economic efficiency

The 1978 *Engineers* case involved the first direct ousting of social factors for those of efficiency.[55] Engineers had agreed to forbid price bidding and contended that competitive bids would lower prices to the point where a socially desirable level of quality and safety was impossible. The U.S. Supreme Court rejected this defence as inappropriate to both corporate and judicial decision-making. The only objective relevant for a company was individualistic profit-maximization. The only factors relevant to an antitrust court were those relating to competitive impact, the prime factor of which was efficiency.[56]

The equity based foundation of U.S. antitrust was removed and replaced with an efficiency foundation focusing on consumers.

Once it was seen that bigness and agreements on price were no longer bad *per se*, it did not take long to argue that bigness was also good.

Bigness enhances economic performance by allowing producers to attain economies of scale and the benefits of cheaper prices to consumers. The focus moved from an emphasis on **rivalry** that lowers prices to **efficiency** that lowers prices. Some of the implications drawn from this shift are:

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[55]*National Society of Professional Engineers v. United States* 435 U.S. 679, 1978.

[56]See Korah, "From Legal Form toward Economic Efficiency: Article 85 (1) of the EEC Treaty in Contrast to U.S. Antitrust", 35 **Antitrust Bulletin**, 1990, 1010 (citing R. Bork, **The Antitrust Paradox**, pp. 7 ss.):

> A consideration of the virtues appropriate to law *as* law demonstrates that the only legitimate goal of antitrust is the maximization of consumer welfare. Current law lacks these virtues precisely because the Supreme Court has introduced conflicting goals, the primary one being the survival or comfort of small business.

K.G. Elzinga, *op.cit.*, pp. 1194-5:

> Antitrust policy, therefore, need not concern itself directly with increasing the purchasing power of the poor, because it accomplishes this indirectly when it prohibits cartels and monopolies in the single-minded pursuit of efficiency.

> ...mergers...produce the economies of scale needed to foster efficiency, productivity, innovativeness and international competitiveness...economic analysis suggests that antitrust laws should be lenient towards mergers.[57]

> The "big is bad/small is good" view of antitrust has been thoroughly defeated. The primary purpose of the antitrust laws is to prevent consumers from paying prices that exceed competitive levels...higher-than-competitive prices constitute unfair takings or extractions of consumers' property.[58]

● The age of consolidation

The shift in economic learning and judicial interpretation seeped through to government enforcement. The antitrust agencies under the Reagan-Bush administrations repudiated structural antitrust enforcement. Unleashed from the mandate of smallness, producers leapt on to the anti-structural bandwagon. In the 1980s, the so-called Age of Consolidation witnessed a mega-merger consolidation frenzy unmatched since the great turn-of-the-century trust movement.

Inevitably, a reaction has set in. Adams and Brock, for example, have produced an exhaustive collection of empirics revealing that the consolidation frenzy caused:

- social dislocations,
- inefficiencies,
- bureaucratic inertia and
- reduced global competitiveness of U.S. industry.

In comparison, smaller operations that were able to avoid being swallowed, flourished and were profitable, even hyper-efficient.[59]

Consequently, the pendulum is beginning to swing again. Due to these effects, Chicago anti-structuralism is increasingly being questioned. There is a

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[57]Walter Adams and James W. Brock, "Revitalizing a Structural Antitrust Policy", **Antitrust Bulletin** (1994), 240.

[58]R. Lande, *op.cit.*, p. 632.

[59]Adams and Brock, *op.cit.*, 1994. However, not all the mergers reduced social welfare. Well-done business restructuring can result in better corporate performance in the long-term.

revival pursued by a number of thinkers to bring U.S. antitrust policies closer to the core equity-based (read "populist") concerns of individualist antitrust.[60]

4.2.4 The U.S. exports antitrust

Prior to the rise and subsequent revision of Chicago anti-structuralism, the U.S. had been exporting both its individualistic competitive philosophy, and its competition laws.[61] The next two sections examine how these two individualistic constructs fared in regimes less motivated by individualism.

5. Japan

5.1 Pre-occupation competition

5.1.1 Communitarian competition

The essence of the Japanese market is communitarian. Relationships are key factors in society and business in Japan. For example, the earliest commercial groups, *zaibatsu*, were family-based structures. Other important factors mentioned by some commentators are the homogeneity of Japan's "race", Japan's resource scarcity and its insularity.

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[60]E.M. Fox, "Antitrust, Trade and the Twenty First Century - Rounding the Circle", **The Handler Lecture**, New York, May 26, 1993; E.M. Fox, The Modernization of Antitrust: A New Equilibrium", 66 **Cornell Law Review** (1981), 1140; E. Fox, "The Politics of Law and Economics in Judicial Decision Making: Antitrust as a Window", 61 **New York University Law Review** (1986), 554; K.G. Elzinga, "The Goals of Antitrust: Other than Competition and Efficiency, What Else Counts?", 125 **University of Pensylivania Law Review**, 1191; R. Lande, "Chicago's False Foundation: Wealth Transfers (Not just Efficiency) Should Guide Antitrust", 58, **Antitrust Law Journal**, 631.

[61]Timberg, *op.cit.*, p. 131:
Since W.W.II, the U.S. has been exporting an intangible...the competitive philosophy, together with the rich and practical experience accumulated in seventy years on applying the Sherman Act and other antitrust laws. The process began when the U.S....as the military occupiers and governors of Germany and Japan...adopted detailed decartelization measures, patterned upon U.S. models, for those countries.

Competition in Japan occurs within the framework of these relationships. These have three effects on the intensity, directness and results of competition:[62]

- First, competition takes place between groups, rather than between, or against, individuals. Competition between groups of merchants, or *za*, has been going on for centuries. Group competition may be intense, but it is not cut-throat and never escalates to the point where it would kill the relationship.

  The Japanese merchant class had its origins...at least 1000 years ago...business men were organized in groupings that took their name, *za*, from the seat or place where the commercial business was transacted....[63]

- Second, competition is less direct and less confrontational. Even the vanquished remain part of the group. Even the most successful merchants remained bound by a class structure that kept them subordinate to the Emperor and his samurai.[64]

  The merchants' position continued to strengthen till the beginning of the Tokugawa era in 1603. Society then became much more rigidly stratified on Confucian lines than it had been, and of the four classes of persons in society the merchants were the lowest.[65]

- Third, the competitive ethic does not tolerate ostentation. Since ostentatious display of the spoils of commercial success was rewarded by confiscation, profits had to be recycled into the group to be retained.

  The merchants with their tightly controlled monopolies prospered financially, but status-wise, they remained oppressed...if they evidenced any excesses their property was confiscated... The merchants,

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[62]Iyori, "Antitrust and Industrial Policy in Japan: Competition and Cooperation", in Saxonhouse and Yamamura, eds., **Law and Trade Issues of the Japanese Industry**, Seattle: University of Washington Press, 1986, p. 61.

[63]Angelo, "Big Business and the Law in Japan - An Historical and Contemporary Conspectus", Victoria: **University of Wellington Law Review**, 1975/6, No. 8, 115.

[64]Ruth Benedict, **The Chrysanthemum and the Sword**, Tokyo: Tuttle, 1954, p. 154.

[65]Angelo, *op.cit.*, p. 116.

> therefore, became a hidden force in the nation... These cultural forces forced the merchant groups underground, to become even more inscrutable and subtle than before.[66]

These factors created a more subtle form of competition in Japan than in the West, a form of competition where the motive of profit-maximization, while still existing, was often subsumed by social factors.

5.1.2 Imported individualistic competition

When the Japanese market was forced open by Western traders, two new concepts arrived along with the trade flows.

- First, the concept of rights began eroding feudal class controls allowing the relative status of merchants to rise. The merchants were provided a strengthened role in Japan; their rising status allowing them to make more demands of government. For example, confiscation of profits by the state was replaced by nationalization of industries.[67]

- Second, the Japanese were exposed to U.S. companies professing the faith of frontier-like and individualistic confrontational competition, which brought in low-priced and tariff-free goods.

- **Cartelization and the relationship-based networks**

Confrontational competition was alien to the Japanese.[68] Japanese merchants demanded protection from confrontational competition, though not from competition itself, and sought to stem their losses through cartelization. The first cartel activity in Japan started with the formation of the Paper Making

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[66]Angelo, *Ibid.*

[67]Angelo, *op.cit.*, p. 118:
The class system was abolished and trading began on a new basis with the nationalization of a number of existing industries, state development of a host of new industries and government control of the nation's financial development.

[68]Ramseyer, "Lawyers, Foreign Lawyers and Lawyer-Substitutes: the Market for Regulation in Japan", 27 **Harvard International Law Journal** (1986); see also Wilks, **The Revival of Japanese Competition Policy and its importance for EU-Japan Relations**, London: Royal Institute of International Affairs, 1994, p. 12.

Federation in 1880, and the Spinning Federation in 1882. In 1907, affected by recession after the Russia-Japan War (1904-5), more cartels were formed and more obvious *Zaibatsu* concerns emerged. Businesses in Japan began calling for pro-cartel laws and their enforcement by the courts. Pro-cartel legislation of 1925 included the Export Association Act and the Important Export Commodities Industrial Association Act.[69]

Consumers and competitors in Japan did complain about monopoly prices that resulted, but did not trace their harm to its root nor suggest that the government enact a competition law. Nor did the courts find price cartels illegal. In decisions from 1907 to 1935, Japanese courts repeatedly decided that a price agreement among competitors was lawful, much in contrast to U.S. legal opinions which held that cartels were *per se* illegal.[70]

- **Cartelization by imperialists**

In Japan, cartels were perceived as a necessary economic bulwark against recessions and international competition, as well as an essential support of the Japanese government's military and political drives to build an empire in Asia. The great trading groups that developed between 1868 and 1945, the *zaibatsu*, were involved in Japan's military undertakings. The grandest of Japan's empire-building schemes was the pre Second World War drive of acquisition, colonization and imposition of imperialism to create a Great Asia Co-Prosperity Sphere.[71]

[69]Similarly, in 1933, the U.S. enacted the National Industrial Recovery Act, which allowed cartel agreements to a certain extent; in Germany, the Act Concerning the Establishment of Compulsory Cartels was enacted to promote cartels and their use by government for economic control. See Iyori, *op.cit.*, pp. 228, 232; Iyori and Uesugi, **The Antimonopoly Laws of Japan**, Milwaukee: 1983, p. 2; and Angelo, *op.cit.*, p. 118.

[70]See, for example: *Nakaguchi et al. v. T Hata*, Osaka High Court., Feb. 15, 1907; *H. Yokoi v. Osaka Shuruisho Dogyokumiai*, Supreme Court., July 19, 1920; *G. Nagai v. Tokyo Yakugyo Dogyokumiai*, Supreme Court., Nov. 26, 1935.

[71]Angelo, *op.cit.*, p. 119.

5.2 Occupation competition policy

During the occupation of Japan, the U.S. Supreme Commander of the Allied Powers (SCAP), sought to undo the strong links between business groups and political power. The SCAP economic and political deconcentration programme had six goals:[72]

- dissolve the top holding companies;
- eliminate inter-corporate stock ownership and interlocking directorates;
- eliminate the influence of *Zaibatsu* families;
- reshuffle executive personnel in combine enterprises;
- break up giant operating companies; and
- enact permanent antitrust laws.

Moreover, the SCAP programme had three main elements:

- A strong dose of democracy: The biggest change was the shift of constitutional authority from the Emperor to the people, and the greater protection of human rights and freedoms. Both were accompanied by significant reforms of the commercial and civil law to meet U.S. standards of democracy and justice based on an equitable common law.
- The separation of state and business: All laws enacted before or during the Second World War promoting cartels and trusts, restricting competition and controlling the market with cooperation between government and business were abolished.
- The deconcentration of business groups.

The breakup of business groups was meant to inject more individualistic competition than had been seeping into Japan over the previous 75 years.

To ensure that groups did in fact reform, the Anti-Monopoly Law (AML) of 1947 was enacted. It represented a strengthened version of U.S. antitrust legislation and gave Japan one of the most ambitious competition laws in the world.

[72]Hadley, *op. cit.*

5.2.1 Super-structuralism: the original draft

The original draft of the Anti-Monopoly Law rested on the three *per se* controls of:

- restraint of trade,
- monopoly, and
- unfair trade practices.

Article 4 prohibited any horizontal agreements on price, quantity or other terms of business. Article 9 forbade holding companies. Unique to Japan, Article 11 set limits (5%) on inter-corporate shareholding and holdings by financial institutions—there is no counterpart in U.S. antitrust laws. Article 13 put limits on inter-locking directorates. These provisions were aimed at busting up the relationships that had built Japanese business.

As a result of this super-structuralist programme, far stronger than the doctor ordered for itself, the Japanese economy was subjected to the most far-reaching trust-busting deconcentration and structural reorganization programme in the post World War economy. Scores of giant Japanese holding companies were dissolved; the two largest of these (Mitsui and Mitsubishi) were divided into some 200 separate firms. Japanese courts and the newborn Fair Trade Commission (JFTC) found cartels illegal *per se*.

5.3 Post-occupation competition

Japanese business resented the forceful demonstration of U.S. competition policy even before SCAP's departure in 1952. Industrial groups and government ministries pointed out that Japan, unlike the U.S., did not have abundant resources and land, where a frontier ethic of individualist competition could flourish. In their view, the new AML provisions were not suitable to Japan and represented a policy to weaken Japanese industries.[73]

5.3.1 Mini-structuralism: Individualistic competition policy vanquished

[73]See William Chapman, **Inventing Japan: An Unconventional Account of the Postwar Years**, New York: Prentice Hall, 1991, p. 103.

Faced with a communist threat in Asia and demands from U.S. businessmen eager for a new market, SCAP backed off its deconcentration programme. SCAP agreed to let Japanese companies consolidate and to make way for U.S. industries to work with Japanese business by means of investment and technical cooperation.[74] This about-face left public opinion in Japan with little appreciation of competition policy.

While the U.S. trustbusters spoke with confused tongues, the Japanese, united for centuries by an ethic of trust-building, were united in their condemnation of trust-busting. Voices representing recently deconstructed industry spoke up immediately following the U.S. withdrawal. In sum, the super-structuralist approach was weakened in three ways.

- **Deletion/Amendment:** First, the strongest and most structural *per se* provisions were targetted for deletion or amendment. Article 4 was weakened to prohibit only substantial restraints of competition. Other *per se* areas were eliminated, such as the deletion of the monopolization provisions under Article 8, while still others were replaced with a test of reasonableness **as viewed from a Japanese perspective.**[75]

- **Exemption:** The second form of weakening was by exemption of business activities from the application of the AML. The year of SCAP withdrawal also witnessed the enactment of sectoral exemptions allowing depression and rationalization cartels. Early examples from the 1950s include: the Coal Mining Industry Rationalization Temporary Measures Act, the Machinery Industry Promotion Temporary Measures Act and the Electronics Industry Promotion Temporary Measures Act. The Ministry of Industry and International Trade (MITI) tried to weaken the application of the AML either by enacting exemptions or by the use of administration guidance to limit so-called **excessive competition**.

[74]Sawada and Brown, "American-Japanese Antitrust Law", 2 **Columbia Journal of Transnational Law** (1963), 92.

[75]Uesugi, "Japanese Antimonopoly Policy: Its Past and Future", 50 **Antitrust Law Journal** (1981), 711.

- **Legislative and Judicial "Reasonableness":** Third, the AML was re-written to emphasize a reasonable concern with dominance, rather than an unreasonable abolition of group-ness *per se*. As prohibitions against groups weakened, cartels were also permitted in depressed or inefficient (rationalisation) industries and exemptions for resale price maintenance were established.[76]

Soon the courts began emasculating the remaining main prohibitions one by one.

- In 1953, in *Asahi Shimbunsh*,[77] the courts limited the prohibition of horizontal agreements to cases involving dominance.[78]
- In *Toho and Shintoho*,[79] the courts removed even this diluted prohibition from vertical agreements, deeming the prohibition of monopolies as only applying to those involving dominant players.[80]

[76]Resale price maintenance (RPM) refers to a vertical price agreement in which a manufacturer-supplier attempts to remove all or part of the re-seller's independent pricing discretion. Retailers charging a lower price than the manufacturer-posted price floor may have to reckon with the loss of distribution privileges. RPM may also take the form of a maximum or a fixed price.

[77]*Asahi Shimbunsha et al v. FTC,* Tokyo High Court, March 9, 1953.

[78]Ariga, *op.cit.*, pp. 452-3:
The *per se* prohibition within article 3 was limited to cases of dominance...no entrepreneur "shall undertake any unreasonable restraint of trade"... The words, in themselves reminiscent of the rule of reason, are defined by the Act in a manner which could, if taken literally, encompass the entire span of Sherman Act section 1...but...the decisions of the Tokyo High Court have restricted the provision to a much narrower scope...[making] it abundantly clear that the unreasonable restraint prohibition of article 3 is limited to cases in which there are...substantial restraints.

[79]*Toho K.K. and Shintoho K.K. v. FTC*, Tokyo High Court, December, 7, 1953.

[80]Mitsuo Matsushita, **International Trade and Competition Law in Japan**, Oxford: Oxford University Press, 1993, p. 87:
The control of a monopolistic situation is not premised on a wrongful *conduct* of an enterprise. As long as there is the monopolistic *structure*...a deconcentration order may be issued. Therefore, this control is a control of structure rather than a control of conduct.

- The court in *Kikkoman* [81] clearly made the structuralist assumption that only powerful enterprises could act anti-competitively.[82]

At the same time, however, the court did note the importance of relationships in Japanese business by allowing that **control** could occur even without direct contact between enterprises, if a strong effect was felt. Finally, the courts also prefaced every area of the control of unfair business practices with a requirement of dominance.[83]

● The focus on dominance

With the focus of the Fair Trade Commission of Japan (JFTC) and courts confined to dominance and structural restraint,[84] less emphasis was placed on trust-busting itself. The inevitable result was a regrouping throughout the 1950s and 1960s. For example, in 1968 two huge mergers were proposed: one involving the three largest paper companies; and the other the two largest steel

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[81] *Noda Soy Sauce Company v. FTC*, Tokyo High Court, 15 December, 1957, Kosai Minshu, 10/10, 1957, p. 743.

[82] Mitsuo Matsushita, 1993, *op.cit.*, p. 117:

> One question is whether or not it is necessary that the enterprise which is engaged in a private monopolization has a certain degree of economic *power*... There is no wording in the Anti-Monopoly Law which clarifies this question. However, by the very nature of private monopolization, it is impossible for a small and weak enterprise to exclude or control the business activity of other enterprises and eliminate competition in a market. Therefore, naturally, it is a large enterprise in terms of market share or otherwise which is capable of committing a private monopolization.

[83] Prohibited **refusals to deal** had to be practiced by a company with a high degree of market share [*Osaka Burashi Kogyo Kumiai*, FTC decision, 20 September, 1955, Shinketsushu, 7 (1956), p.20; Mitsuo Matsushita, *op.cit.*, pp. 150-1: "It seems that a high degree of market share is required in order to hold that an individual refusal to deal is unlawful."]. **Price discrimination** enforcement would only focus on large leading manufacturers [*Toyo Linoleum*, FTC decision, 7 February, 1980, Shinketsushu, 26 (1980) 85]. **Tying** is only prohibited if practiced by sellers with "sufficient economic power" [*Textbooks*, FTC Decision, 11 February, 1964, Shinketsushu, 12 (1965), 100; *Farmers' Cooperatives*, FTC Decision, 12, December 1963, Shinketsushu, 39; Mitsuo Matsushita, *op.cit.*, pp. 154-5]: a **tie-in contract** is held unlawful if it is used by the seller of a commodity with sufficient economic power with regard to the tying commodity. **Exclusive dealing** is only a concern if it is practised by "an enterprise with strong market power" [*Muto Kogyo*, FTC Decision, 22 November 1974, Shinketsushu, 21 (1975), 148; Matsushita at 155]. **Vertical territorial restrictions** require that the imposer be a powerful enterprise...." [Mitsuo Matsushita, *op.cit.*, p. 158; see also 1991 JFTC Guidelines].

[84] See I. Prakash Sharma, "The Abuse of Dominance: A Comparison of National Competition and Trade Regimes", **Policy Staff Paper** No. 96/01, Ottawa: Foreign Affairs and Internatinal Trade, (forthcoming 1996).

companies in Japan. The JFTC rejected both. The paper merger was abandoned. But with the support of MITI, the steel companies pursued their plans. Although the JFTC objected, after intense pressure from business and MITI, it agreed. Thus, Nippon Steel came into being.[85]

It was only once reconstruction was safely underway that a process of revitalization of the AML began. Exemptions were reduced drastically. From a thousand in 1963, exemptions declined to 528 in 1977. Also, the number of export cartels decreased under the Export and Import Transactions Law from a peak of 209 in 1969 to 53 by 1982. At present, there are only 11 export cartels involving major manufacturers. Ironically, many of these remaining export cartels responded to demands by other countries for voluntary export restraints against competitive imports from Japan.[86]

- **The hesitant return of *per se***

The most important development, however, was the amendment of 1977. The original *per se* structural control of monopolistic situations, purged in 1953, was revived in a different form that also considered not only shares, but also prices and profit rates. A reporting system was introduced whenever prices of a product went up simultaneously throughout the market. Within three months of such monitoring, the JFTC could order the major enterprises to explain why the prices had been raised.[87]

The introduction of a cartel surcharge created a pay-as-you-group fee that tried to capture the gains of the anti-competitive relationship. This surcharge made the fines a percentage, which was raised from 2% to 6% in 1991, of sales during the cartel period. This was one area where the JFTC addressed the root of anticompetitive effects in communitarian competition.

5.4 The Japanization of competition policy

[85]See Wilks, *op.cit.*, p. 9.

[86]Iyori, *op.cit.*, p. 79.

[87]See Mitsuo Matsushita, 1993, *op. cit.*, p. 83.

● The failure of U.S.-style antitrust in Japan

The failure of U.S. antitrust in Japan and the reformulation of a Japan-specific competition policy was based on a cultural clash fought in three arenas: political, legal and economic.

The strong U.S. antitrust system was based on a distrust of big business groups and functioned in an individualistic system supported by strong democratic and individual rights. From a political perspective, such a competition regime was thrust upon Japan, a country that culturally rested on communitarian pillars. According to the norms of individualist politics, Japan was not so well off. Democracy there was only struggling to be born; there was no tradition of civil liberties; giant business historically controlled the major political parties; and for the longest time there was no effective antitrust law on the statute books.[88]

The framers of the AML relied on U.S. antitrust ideas with roots in the individualist tradition largely alien to the cooperative business philosophy of Japan. Little effort had been made to understand the Japanese market before the AML was drafted and imposed.

Interestingly, the imposition of this programme attracted political opposition in the U.S.. Equity theorists and politicians argued that it did not make sense to recommend the wholesale dissolution of large conglomerates in order to achieve a more Jeffersonian landscape. Economists in the U.S. questioned the efficiency of deconcentration, given the unknown social costs of such disruptions.

● The return of communitarian equity and freedoms

The U.S. view of freedom emphasizes independence. Independence of the market, or laissez-faire, means freedom from control. In Japan, however, the term laissez faire means the freedom of government to favour some businesses and the freedom of businessmen to contract for a wide variety of restrictive

[88]Hadley, *op.cit.*, p. 294; and Karel von Wolfern, **The Enigma of Japanese Power**, New York: Knopf, 1989.

practices. Naked price theory and self-interest do not dominate the market; relationships are important too. The U.S. SCAP trust-busters ran right into this difference. In applying the AML, SCAP viewed Japan's combines as tough, unfair competitors—unfair, that is, according to U.S. rules of the game. Through Japanese eyes, such combines offered substantial benefits in terms of the stability of relationships and security of supply and labour.

This different understanding of fairness in the two countries explains many economic disputes between them. While it is true that an economy is an economy, whether individuals act on oriental or occidental avarice, the relative weight given to individualism or communitarianism skews the factors relevant to any economy. The next sections address this tension.

5.5 Competition enforcement in Japan

In Japan, private informal dispute settlement is more important than the use of public and formal laws to settle disputes.

● The role of public law

In the West, the law has been viewed as protecting freedom and equality. While sharing this principle, the law in Japan is, by contrast, considered primarily as an instrument of government control. Since the government-business relationship in Japan has traditionally involved negotiation and compromise, the cooperative proclivity usually makes resorting to law and litigation undesirable.[89]

● "Wa" over war: the role of private law

Informal agreements are the norm in Japan. So too are informal dispute resolution processes. The knee-jerk response to disputes in relationships in Japan is not "Sue". It is the very last thing that would be attempted, if at all. Formal contracts are less necessary in Japan. Parties to an agreement often have

[89]Iyori, *op.cit.*, p. 62.

a relationship going between them already. Japanese society prefers informal but real agreements with people, over formal official paper-exchanges.[90]

The rarity with which the Japanese go to law is well-established. It has been attributed to the absence of a legal tradition analogous to Roman law and more particularly to the preference for harmony and conciliation in a Confucian culture. Japan is a non-litigious society. Legal action is used rarely and as a last resort. Few suits are brought if there is a breach of contract.[91]

5.5.1 Private informal dispute resolution

The existence of Japanese lawyers, law suits and courts show that the cultural barrier is not all-powerful, however. It may be a higher first hurdle to cross, but it is still only a hurdle. A kind of cost-benefit analysis is taken when anyone considers litigation. Potential litigants sue only when the amounts they may recover, multiplied by their probability of success, exceed their litigation costs. One cost component in this calculus that is more important in Japan than in the West, however, is the risk of jeopardizing the relationship at the heart of the dispute.

Other hurdles have been institutionalized: the dearth and expense of lawyers, high court filing fees and a limited class action capability, all chill formal dispute resolution. The AML itself also limits the right of private action. The result: between 1947 and 1985, only seven private antitrust actions were

[90]The following offer excellent, real-life descriptions of the Japanese approach to negotiation and agreements: Zimmerman, **How to Do Business with the Japanese**, Tokyo: Tuttle, 1985; Athos and Tanner, **The Art of Japanese Management**, New York: Warner, 1981; Vogel, ed., **Modern Japanese Organization and Decision-making**, Tokyo: Tuttle, 1975; James C. Abegglen and George Stalk, ***Kaisha: The Japanese Corporation***, Tokyo: Tuttle, 1985; March, **The Japanese Negotiator: Subtlety and Strategy Beyond Western Logic**, Tokyo: Kodansha, 1989.

[91]For example, a study of Tokyo taxicab companies showed that of a total of 2,567 accidents causing physical injury or property damage, only 2 cases were filed. See Zimmerman,*op.cit.*, p. 93, and Wilks, *op.cit.*, p. 15.

brought in Japan, none successful, compared with 9,000 in the same time period in the U.S.[92]

When society sets up a system of governance, it chooses measures that reflect its preferences. The cultural aversion to litigate in Japan is the prime mover behind these hurdles.

5.5.2 Public informal dispute settlement

The private preference for informal dispute settlement extends to the public sphere, especially in competition policy. Japanese government enforcement of the AML has been quite limited by U.S. standards. While the AML empowers the JFTC to take any measures necessary to eliminate acts in violation, there are few such measures available. Injunctive relief, contempt, criminal sanctions and other orders are either non-existent or of a very narrow scope. As a result of the weakness of formal sanctions, Japanese government officials, particularly those with the JFTC, are forced to rely on extra legal sanction.

Regulatory statutes drafted by SCAP authorities, such as the AML, almost invariably contain extensive enforcement provisions reflecting U.S. practice and administrative powers. The lack of a contempt power by Japanese courts, however, precludes effective formal legal enforcement. The investigatory powers of Japanese government agencies are nowhere nearly as extensive as administrative agencies in the U.S.. If criminal penalties are not a realistic deterrent to corporate immorality for the U.S., there seems little chance for their efficacy in Japan.

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[92]The cultural antipathy for formal, legal confrontational controls reduces the demand to go to law, but also reduces the supply of legal facilitators (at last count, there were little more than 12,000 lawyers in Japan), and the supply of legal means to go to law. While demand for legal redress and supply of legal redress are both reduced, price is still high, because demand is greater relative to supply. Both court filing fees and lawyer fees are based on a percentage of the claim (i.e., the amount *claimed*, not eventually awarded). Class actions are almost impossible to coordinate, file and win in Japan. Class action suits are extremely difficult to file because of a very heavy burden of proof required of plaintiffs; not a single case has been won by plaintiffs since 1945. Private damage suits are allowed under section 26 of the Anti-Monopoly Law, but damages are only recoverable after the JFTC has successfully established a violation. Ramseyer, *op.cit.*, pp. 617, 627; see also Yamamura, *op.cit.*, pp. 56-7; Wilks, *op.cit.*, p. 16.

- **The lack of criminal sanctions in Japan**

The effective use of criminal sanctions to control corporate conduct in Japan is a close to impossible task. Criminal prosecutions engender severe political and intra-agency conflict as a result of the clientele relationship between each economic ministry and the industries within its jurisdiction. Resort to criminal sanctions is similarly precluded except in rare instances by the social density that results from the intricate personal ties that connect the leaders of Japanese business, politics and bureaucracy. Mandated remedial measures are considered legally binding only with regard to the violations set out in the facts of the decision.

Informal control is common to all legal and antitrust systems, but seems ubiquitous in Japan. The cultural proclivity for deference makes even the limited array of formal measures less necessary to command obedience. Such a proclivity is not all that is at work in informal enforcement, however.

- **Prompting voluntary compliance**

The regulated businesses are more likely to obey regulations with which they agree. The probability of compliance increases with participation in the process of regulation. Administrative guidance, the most common form of Japanese informal enforcement, is no different.

All legal systems depend upon voluntary compliance with the law, from the payment of taxes to regulatory control by official suggestion, advice, recommendation or pointed direction. This approach is not only common to all legal systems, it is indeed the most common form of law enforcement including in the U.S. (although prosecutions **are** more common in the U.S. than in Japan).

- **Informal ways of the JFTC**

The real influence of antitrust occurs unseen through negotiations and threats to deter mergers and other actions, and to intervention in regulatory cases through informal persuasion, by threatening to go to court or through testimony at formal public hearings. The same could be said for Japanese antitrust enforcement. The vast majority of all antitrust violations investigated by the

JFTC are resolved informally. Whether labeled administrative guidance or informal enforcement, and whether carried out by the JFTC, MITI, or the U.S. FTC and Justice Department, the process is the same.

The two main means of informal enforcement used by the JFTC are publicity and the administrative surcharge. The JFTC regularly publishes its decisions and tolerates media reporting of its searches. Such publicity deters by relying on the moral suasion accompanying a perceived violation of the public order. Publicity has been the most effective deterrent; the surcharge the most effective sanction. It directly responds to the root behaviour, and is thus arguably more acceptable to the culprits than a more arbitrarily assigned fine.

- **Enforcement through administrative guidance**

Administrative guidance is not peculiarly Japanese, therefore, but its ubiquity is. It is a product of Japan's particular historical and social context and endemic as an aspect of the Japanese economy. Although all major studies in English or German recognize that practices analogous to administrative guidance can be found in the West, most emphasize the cultural factors that seem to explain administrative guidance as a peculiar Japanese institution. The underpinnings for administrative guidance are in the neo-Confucian deference to authority and the related desire to maintain harmony and cooperation and to avoid adversarial posturing, in other words, in the special social psychology of the Japanese.

A community or individual sense of the legitimacy of government actions and policies may determine in particular instances whether a party will comply or not. Both the aim of assisting industry and a lack of strong legal sanctions or other forms of formal legal coercion in effect compel officials in Japan to negotiate and seek compromise with respect to policies they want to implement. Japanese industrial policy is comprised more of a series of responses to immediate economic conditions and events than a carefully designed plan implemented by effective government persuasion.

5.6 Corporate governance in Japan

Both the original and present focus of U.S. antitrust emphasizes the distributional inequity of a monopoly's rent transfer from consumers to producers. Since high prices exist in Japan, it is plausible to infer monopolistic pricing is occurring. The crucial question, however, is whether the same distributional inequity is present too. Such is likely in an individualistic organization, because the profits extracted are transferred to shareholders or management.

Such a transfer is not as great in a communitarian organization, however. If monopoly profits are being extracted, they are not necessarily distributed to management or shareholders to the same extent.[93] Bereft of the discipline of the requirement of short-term dividend payouts, Japanese companies use their profits to maintain their internal and external relationships. The distribution of these unfair rents within companies tends in Japan to be a good deal less unequal than it would be in the U.S.—with shareholders seeing less of the profits to begin with and the dispersal of wages and salaries being much more compressed. Workers do not get more, necessarily, but there is more equality from the president down to the assembly line.

Keiretsu or *zaibatsu* structures defined by their tightly- but invisibly-knit relationships[94] are not unfair from the Japanese economic perspective. Instead they mirror different freedoms: of contract, of association and of playing with one's own team.[95] *Keiretsu* forgo possible short-term savings on price offered

[93]There is some evidence that the fortunes of Japanese executives are more sensitive to low income but less sensitive to stock returns than those of U.S. executives. See Steven N. Kaplan, "Top Executive Rewards and Firm Performance: A Comparison of Japan and the United States", **Journal of Political Economy**, June 1994 (102): 510-46.

[94]See Goto and Suzumura, "*Keiretsu*: Inter-Firm Relationships in Japan", a paper presented at the Workshop on Competition Policy in a Global Economy, University of California, Santa Barbara, January 8-9. 1993: *Keiretsu* are identified by four relationship-related factors: cross-shareholding, in that each member holds stock in the others; inter-locking directorates, each member has a seat on the board of the others; each member tends to borrow from financial institutions within the group; and each tends to purchase material from within the same group. See also I. Prakash Sharma, "Japan Trading Corp.: Getting the Fundamentals Right", **Policy Staff Paper**, No. 93/16, Ottawa: Department of Foreign Affairs and International Trade, December 1993, pp. 22-7.

[95]Ely Razin, "Are the *Keiretsu* Anticompetitive? Look to the Law", 18 **North Carolina Journal of International and Commercial Regulation**, (351) 1993.

from non-*keiretsu* sources of inputs, for the sake of the relationship of the group. This relationship offers savings from reduced transaction costs associated with imperfect knowledge. *Keiretsu* source internally, unless an externally sourced input offers savings substantial enough to offset any cost to a relationship.[96] The economics is the same. However, the weight of relationships in Japan skews corporate decision-making away from "mere" price concerns. In Japan, such in-group sourcing is actually not collusion. It is just a refusal to act on price.

Those who object to the "closed" nature of the Japanese market label the relationships between *keiretsu* groups anticompetitive. Nonetheless, not only can they allow a great deal of competition, they can be but a pre-requisite to enter the competition. Non-*keiretsu* **Japanese** firms succeed because their own relationships and longer time horizons allow them to sacrifice profits to enter the market.

Foreign companies, dominated by the short-term profit motive, cannot justify the investment necessary to stay the course, and resign themselves to non-entry. In shutting themselves out, they deny the Japanese market of what positive competitive effects their entry might bring. Since that loss is well compensated by strong domestic competition, however, some have suggested that there is little difference, for consumers, between prices resulting from a *keiretsu* "closed" market, and those resulting from a "freer" market. From the perspective of the consumer, there may be little difference between an industrial structure that fosters competition among a stable group of established firms through diversification into new product areas and one that encourages similar rivalry through easy firm entry.

Foreign companies wishing to enter the Japanese market should not automatically label the relationships they refuse to build as anticompetitive, nor necessarily join the chorus calling for increased antitrust enforcement against them. They should instead focus more on increasing their efforts to build

[96]Dore, *op.cit.*, p. 372: "it would be surprising if the efficiency gains from these customer-market arrangements - stemming from increased trust, extra cooperativeness induced by expectations of loose reciprocity, savings on litigation, etc. - did not outweigh any welfare loss occasioned by sub optimal resource allocation".

relationships that will allow them to enter the fray. If they call for anything, it should be the right to form relationships with Japanese companies, and among themselves, that will allow them to compete over the long-term.

5.7 Japanese competition policy in U.S.-Japan trade disputes

During the Structural Impediments Initiative (SII) talks of 1989-90, the negotiations between the U.S. and Japan also focussed on the AML and its enforcement in Japan. The SII package included issues such as: (a) price differences between Japanese products sold in foreign markets and the market in Japan; (b) *keiretsu*; and (c) the amendment and enforcement of the AML.

● The U.S. demands

The U.S. contention was that the removal of private trade barriers such as restrictive business practices was essential to improve access for U.S. corporations in the Japanese market. The U.S. insisted that the AML would have to be amended and actively enforced. To restore free markets in Japan, private barriers would have to be challenged by vigorous enforcement of the AML. The SII was to be implemented by 1993.

The Japanese government responded by relaxing regulation under the Large Scale Retail Stores Law. The AML was amended to increase Administrative surcharges (from 2% to 6%) imposed on price cartels; criminal fines on corporations were increased from the maximum of five million yen to 200 million yen. In 1991, the JFTC issued "Distribution Guidelines" dealing with restrictive business practices between suppliers, subcontractors and manufacturers and from manufacturers to dealers and consumers.[97]

● The renewed U.S. demands

In 1993, U.S. bilateral trade policy toward Japan, now renamed the **Framework Talks**, moved further from a competition policy focus toward

[97]See Mitsuo Matsushita, "Harmonization of Competition Laws Through Bilateral Trade Negotiations: The Japanese Experience", *New Dimensions of Market Access in a Globalizing World Economy*, OECD Documents, Paris: OECD, 1995, pp.129-37.

convincing the Japanese to agree to numerical market shares for foreign goods and services in the Japanese market with the aim of increasing U.S. market penetration. Target shares for foreign products in the Japanese market were related to sectors such as automobiles, parts and components of automobiles and insurance. Japan resisted the U.S. tilt to managed trade with a reform programme in March 1994, addressing issues such as deregulation, competition policy, direct investment into Japan, government procurement and increased imports.

Under this programme, the number of investigators at the JFTC will increase, and the JFTC is required to issue draft guidelines on the prevention of bid-rigging and on the activities of trade associations, as well as instituting a review of laws which exempt various types of cartels from the application of the AML, with the view to abolishing them in five years.[98]

- **U.S. demands undermine competition policy in Japan**

The U.S. approach under the Frameworks Talk, however, is antithetical to the basic principle of competition policy. If the Japanese government were to agree to numerical targets for U.S. products sold in Japan, the Japanese government would have to suspend the functioning of free markets in Japan and require Japanese companies to buy the agreed volume of goods from U.S. corporations. Trade associations in Japan might have to co-ordinate their purchases by engaging in anticompetitive collusive activities. Competition policy in Japan would be undermined. It is contradictory to seek to implement a market-sharing programme while promoting free markets in Japan through effective enforcement of the AML.

U.S. trade policy under the SII, perhaps, had the useful effect of promoting competition policy and freer markets in Japan. In contrast, under the Frameworks Talks, U.S. trade policy may lead Japanese corporations among themselves and in deeper cooperation with the Japanese government to engage in anticompetitive business arrangements. In this case, U.S. trade policy toward Japan would undermine efforts to promote more effective enforcement of competition laws in Japan.

[98]See Sharma, Thomson and Christie, *op.cit.*, 1994, Annex A.

6. European Union

6.1 European capitalism, competition and occupation

Structural U.S. antitrust arrived in Europe in much the same way that it arrived in Japan. Its main policy beachhead was in Germany. Following the Second World War, the U.S. Occupation there found a very similar cooperative framework to what U.S. forces confronted in Japan.

German capitalism is more like that of the Japanese. Rather than freedom from control by government, it promotes the freedom to associate, regulated by justice.

Hayek noted that the German ethic of discipline evinces a lack of individualistic behaviour that is more akin to that of the Japanese, in its acceptance of order and personal sacrifice to forward the group over individual members.[99] Indeed, Japan and Germany are countries noted for their careful organization of teams, at all levels of business and business-government interaction.

The German High Court in 1897 ruled that cartel agreements were lawful and binding under the freedom of association accorded workers and businesses under German law. While the German and Japanese approach to cartels differed from the U.S., the German approach was more akin to permission, than the direct prescription of cartels in Japan.

The cartels that formed in continental Europe had a looser structure than in the U.S.. The U.S. Occupation, however, applied its own antitrust ethic to what it assumed were "problems". Detailed deconcentration measures sought to separate the links between companies, and between business and government, that the Occupation assumed had contributed to the strength of Fascist and Nazi efforts at empire building.

[99]Hayek, *op.cit.*, 1947, pp. 148-9.

Again, the U.S. back-tracked to allow the rebuilding of the European economy with the assistance of U.S. business, partly because of the rapidly emerging Soviet threat. As in Japan, this undermined the credibility of the deconcentration measures.[100]

Soon after the formal end of U.S. Occupation, as in Japan, Germany made amendments to the U.S. imposed deconcentration statute. Germany allowed rationalization and depression cartels. Indeed, the amendments that occurred in Japan in the early 1950s were influenced, even driven, by German precedents. As a result, today, Japanese antitrust law can be understood accurately only when read in terms of German rather than U.S. practice.[101]

The strongest movement growing in Europe after the Second World War was the 1957 Treaty of Rome which created the European Communities. The European Commission took a different approach from that of the U.S. Occupation. This movement also sought an end to political and military struggles that had devastated Europe for centuries. **European cartel laws tended to follow the German pattern**, requiring registration, correcting abuses only occasionally and, in many instances, encouraging the formation of cartels when market conditions proved to be unstable.

Hawk has argued that U.S. antitrust ideals indirectly influenced the drafting of European competition policy through their direct effect on German competition policy. However, as the discussion above suggests, Hawk's argument should be considered contentious. In this view, EU competition law was born in 1958 of transatlantic parents. Its European mother was the basic Treaty goal of market integration. Its father (or godfather) was U.S. antitrust law and theory which influenced the drafting of Articles 85 and 86 of the Treaty of Rome through German law and thought.[102]

6.2 The European integration project

[100]See Scherer, *op.cit.*, p. 29; Iyori, *op.cit.*, p.246; Doern, *op.cit.*, p.25; and Timerg, *op.cit.*, p.25.

[101]See Iyori, *op.cit.*, p. 238; and Haley, *op.cit.*, p. 473.

[102]B. Hawk p. 53; F. Scherer, p. 28 .

The essence of all European Union legislation is to integrate economies of Member States. Economic integration is a goal, but also a means to political integration, through the reduction of the disparities that have historically led to political struggle in Europe.[103]

At a philosophical level, this process is applying a form of communitarian relationship-building to extremely individualistic societal structures. The empire-building motive may have arisen periodically in Europe epitomized or propounded by the Caesars, Napoleon, Hitler and even Marx and Lenin; however, it never prevailed. One reason for this is Europe's geographically segmented mini-communities. Their homogeneity may have allowed them to grow internal communitarian systems, but they could never succeed in building or imposing such relationships over other European peoples.

In contrast, the European integration project is using the communitarian idea of relationships to link the formerly isolated markets. It differs from prior political and military attempts that sought the imposition of an order from the top down through subjugation, in that it seeks union from the bottom up, through political subsidiarity and economic linkages at the corporate level.

6.3 Competition and competition policy in an integrating market

In two ways, competition is an important tool of integration.

- Free trade increases competition and increases the field of vision of individual actors in the market. They must be more concerned about other actors, both through the increased discipline of competition and through increased opportunities for cooperation.
- Through recognizing these opportunities, individual actors can unite and grow to capture greater economies of scale that make them more efficient.

In this view, competition policy's role in the integration process is to allow cooperative growth. It is a major and necessary tool of integration.

[103]Article 2: The main task being "progressively approximating the economic policies of Member States". The Preamble identifies the Community's goal as: "an ever closer union"; Article 2: "a common market"; see also Article 3 (a) - (g), 8 and 8a. Article 4 expressly entrusts this quest to key EU institutions.

Competition policy contributes to this process by allowing market forces to re-allocate production efficiently in the newly expanded market across national (and nationalistic) borders.

> The EU has established that the primary goal of the competition articles is the elimination of economic barriers among Common Market states and the promotion of the "free flow of goods" in a single, unified market.[104]

The integration goal is a long-term project, the benefits of which may not be realized by individualistic economic actors blinkered by the short-term. The increased discipline of competition over industries formerly protected by national borders itself creates an incentive in them to re-segment the market through anticompetitive restraints. Such anticompetitive activity can be profoundly frustrating to the process of integration. Articles 85 to 94 of the Treaty of Rome were directed against cartels, restrictive agreements and abuse of dominant position, all of which were regarded as undermining the process of attaining integration through trade within the EU. Thus, a major task of the EU is in ensuring that competition in the broader common market is not distorted.[105]

European competition policy helps to create a market that is common and free of public or private restraints. Being paramount, the integrationist urge has had a profound impact on the priorities of European competition policy, distinguishing them from those of domestic competition regimes.[106]

6.4 European competition policy

6.4.1 Integrationist anti-structuralism

The first profound impact of the Treaty of Rome on competition policy was in the choice of approach. The drafters of the EU treaty did not follow the

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[104]Kalmansohn, "Application of EEU Articles 85 and 86 to Foreign Multinationals", 2, **Legal Issues of European Integration**, (1984), 2.

[105]Treaty of Rome, Article 3(f).

[106]See Wyatt and Dashwood, **European Community Law**, 3 ed., London: Sweet & Maxwell, 1993, pp. 377-8; Kalmansohn, *op.cit.*, p. 3; van Bael and Bellis, **Competition Law of the EEU**, 2 ed., Bicester: CCH Editions, 1990, p. v; and Weatherill and Beaumont, **EU Law**, London: Penguin, 1993, p. 592.

U.S. structural model. In their view, European markets were inefficient, not because of dominant companies but because of the confines of national boundaries which maintained companies of sub-optimal size and efficiency.[107]

The solution was to allow these companies to grow to attain economies of scale and size. Moreover, as the companies grew, their scope of influence would cross national borders. Corporate integration would thus lead to regional integration.

> [T]he founders of the Community did not oppose bigness...business units within the Common Market were often below optimal scale as a consequence of the trade barriers that limit the size of available markets... By breaking down the barriers at Member State lines, the drafters of the Treaty hoped to provide markets big enough to support the larger units that efficiency demanded... Mergers between firms in different Member States could help to integrate the economies of the Member States.[108]

Bigness was not an absolute, however. If it were, then competition policy might well have been irrelevant. The role that competition policy took in Europe was to allow growth up to the point where it created dominance tending toward inequity, inefficiency and re-segmentation of the European market. The concerns of equity and efficiency, however, were coloured by that of integration.

6.4.2 Integrationist equity

The focus on integration did not exclude equity concerns. EU competition policy is the most forthcoming in its statement of concern for the welfare of its citizenry. It specifically enumerates multiple policy objectives within the Treaty which allow a special place for concerns over equity.

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[107]Timberg, *op.cit.*, p.135:
First, European antitrust policy did not arise out of a background of indignation against the iniquities of monopoly. In fact, the sentiment in France and many other European countries was that their business enterprises were too small to be efficient.

[108]See Fox, "Monopolization and Dominance in the United States and the European Community: Efficiency, Opportunity and Fairness", 61, **Notre Dame Law Review**, 982-4.

First, the very notion of competition in Europe includes political and social values in correcting inequity.[109] The Treaty preamble urges the improvement of living standards through the reduction of differences:

> The Preamble includes the following objectives: "Affirming as the essential objective of their efforts the constant improvement of the living and working conditions of their people... Anxious to strengthen the unity of their economies and to ensure their harmonious development by reducing the differences existing between the various regions and the backwardness of the less favoured regions...." Article 2 speaks of "an accelerated raising of the standard of living", and "progressively approximating the economic policies of Member States".[110]

- **Surplus transfers**

Anticompetitive activity can work against integration by creating and maintaining economic disparities. To prevent these, competition policy in Europe is concerned with wealth transfers caused by anticompetitive activity. Such transfers became even more possible in Europe due to the four freedoms of movement of people, goods, services and capital.[111]

Concerns about wealth transfers are inherently distributive. European competition policy considers the wealth transfers from consumers to producers and from the weak to the strong.

- **Small business**

In general, European competition policy promotes bigness. However, it also makes specific provision for the welfare of small business, which it regards as a mainstay of the economy. Freedom of activity for small business is not to

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[109]Barry Hawk, "The American (Antitrust) Revolution: Lessons for the EEU?", **European Union Law Review**, (53) (1988), 54.

[110]Korah, "From Legal Form toward Economic Efficiency - Article 85 (1) of the EEU Treaty in Contrast to U.S. Antitrust", 35 **Antitrust Bulletin**, (1990), 1009-10.

[111]Article 3 (a): the elimination, as between Member States, of customs duties and of quantitative restrictions on the import and export of goods, and of all other measures having equivalent effect; and

Article 3 (c): the abolition, as between member States, of obstacles to freedom of movement for persons, services and capital.

be constricted by the activities of more dominant actors. Thus, European competition policy provides protection for weak and small operators against excessive use of market power by dominant firms.

- **Consumer welfare**

The Treaty contains a specific provision concerning consumer welfare. The Member States may want to adopt a pro-producer stance by promoting corporate concentration, but Article 85 will come in their way unless, *inter alia*, consumer welfare gains are demonstrated. The objective is not to allow the integrationist-oriented increase in producer welfare to trump consumer welfare. A justification for combinations to distort competition is allowed only where a fair share of the benefits is passed on to consumers.

6.4.3 Integrationist efficiency

Efficiency concerns have their place in European competition policy. Besides the EU institutions, the major tool of integration is the market. A withdrawal of barriers frees market forces to re-channel and flow across state lines. While freed, they are not unfettered. The Treaty drafters realized this.[112] The EU accepts activities that are inefficient, inequitable and anticompetitive in the short-term, but that lead to an integrated market that is efficient, equitable and competitive in the long-term. The nature of EU law makes this possible.

6.4.4 Integrationist law

The two most obvious results of the paramountcy of integration in EU law are its laxer approach to horizontal cross-border arrangements and a stricter approach to vertical restraints that divide markets.

[112]Cappellitti, Seccombe and Weiler, "Integration through Law: Europe and the American Federal Experience, A General Introduction", in **Integration Through Law** (1), Book 1, p. 6.

- **Laxer treatment of horizontal agreements**

Horizontal agreements within national boundaries are prohibited in Europe, for the traditional competition reasons that they restrict competition, reduce efficiency and subvert the market. They may also restrict integration and subvert the common market. Since competition is a means to integration, any agreement that reduces competition may also have anti-integration effects. This is especially so for agreements on share and dealing that divide a national market between competitors.[113]

Horizontal agreements between competitors from different Member States have received more lenient treatment. The idea is that their short-term anticompetitive effect may be offset by their relationship-building effect: the increase in cross-border corporate activity leads to regional integration and longer-term efficiencies. Indeed, the EU view has been that such agreements are a proof that relationships have been built and that integration is working. For example, the EU Commission tends to allow seemingly anti-competitive cross-border mergers since they are evidence that the market is integrating. For these mergers, the EU is less interventionist that would be a purely domestic antitrust regime.

- **Stricter treatment of vertical restrictions**

European competition policy best reveals its integrationist concern in its approach to vertical agreements. Market partitioning agreements are the most serious of all EU competition policy breaches. As Member State barriers are dismantled, it becomes increasingly important to watch that companies do not carve up the market.[114]

Since cross-border trade drives the integration of the market, parallel imports are a prime obsession of the European Union. Due to the extra discipline of competition they bring, producers often seek to foreclose such

[113]See Kalmansohn, *op.cit.*, p. 13; and Claus-Dieter Ehlermann, "The Contribution of EU Competition Policy to the Single Market", **Common Market Law Review** (1992), 257-82.

[114]Weatherill, *op.cit.*, p. 594.

imports through territorial restrictions. Export bans, for example, segment and preserve markets for suppliers. As such, they are a threat to integration and freedom of movement in the market.[115]

- **Article 85 of the Treaty of Rome**

Article 85 prohibits cartels and restrictive practices that are both horizontal and vertical restraints of competition between Member States. Vertical restrictions are the prime target for enforcement, however. Europe's obsession with these restrictions is more intense than would be the case in a market that is already integrated. The U.S., for example, tends to prohibit most vertical restrictions only when they are the result of anti-competitive horizontal agreements.

The EU rules are stricter with respect to a broad range of agreements and practices, such as territorial restrictions along national boundaries and export bans on trade between Member States. Under U.S. law, territorial restrictions are generally upheld as reasonable. The U.S. Supreme Court in *Sylvania* declared such deals permissible under antitrust law. The Union prohibits deals which involve distribution systems that compartmentalize the common market along national lines. In other words, the EU has established a more-or-less *per se* approach to intrabrand territorial market restraints. This approach can be inconsistent with a pure economic efficiency standard; however, it is eminently integrationist.

In the EU, vertical restrictions are in themselves anticompetitive and have been struck down time and again.[116] Their condemnation under Article 85(1) is immediate, unmitigated by other concerns. For example, the EU makes no

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[115]Wyatt, *op.cit.*, p. 404, (citing *Italy v. Council and Commission*, **European Union Review**, (1966), 408): An agreement between producer and distributor intended to restore national partitioning in trade between Member States would be such as to run counter to the most fundamental objectives of the Community... vertical agreements represent a serious threat to the unification of the market.

[116]Kalmansohn, *op.cit.*, p. 11 (citing *Nungesser KG & Eisele* v. *Commission*, **European Union Review**, (1982), 2015; *BMW Belgium SA and others* v. *Commission*, **European Union Review** (1979), 2435; *Centrafarm BV and de Peijper* v. *Sterling Drug*, **European Union Review** (1974), 1147; *SABA*, 1 **Common Market Law Review**, (D61), 1976; *Van Zuylen Freres v. Hag AG*, **European Union Review** (1974), 731; and *WEA/Filipacchi*, **Common Market Law Review** (1973), D43.

enquiry into market power or possible economic justifications or efficiencies before condemning export bans. This failure may reflect the EU's willingness to sacrifice distribution efficiencies in order to achieve and advance market integration, that is, to accept possible short-term efficiency losses to achieve perceived long-term gains from a single market.[117]

- **Defence: Artice 85(3)**

Article 85(3) allows an exemption from the prohibition in Article 85 for anti-competitive agreements which offer offsetting efficiencies. While the *per se* prohibition may seem diluted by the presence of this exemption, the *per se* level of the prohibition itself is not reduced. The efficiency analysis is made only after the integration calculus has been made.

The efficiency exemption is itself limited by equity concerns in its own operation. A significant test for the granting of an Article 85(3) exemption is that consumers receive "a fair share of the resulting benefits", an eminently distributive concern. While the strength of this check of equity on efficiency has arguably been diluted somewhat, commentators on European competition policy agree that first, the dilution is inappropriate, and second, that the efficiency exception is still dominated by the integrationist concern within Article 85(1) itself.

After the *Synthetic Fibres* case, some suggest that, given economic advantage plus persisting competition, the fulfillment of the consumer-benefit criterion is presumed to follow. This is not, however, acceptable as a reading of Article 85(3), which insists that separate attention be devoted to the consumer interest.[118] Since the amelioration of consumer living standards is a tool for uniting the Communities, EU integration is still supreme.

[117]Hawk, *op.cit.*, p. 55.

[118]See also Korah *op.cit.*, "From Legal Form toward Economic Efficiency - Article 85 (1) of the EEU Treaty in Contrast to U.S. Antitrust", 35 **Antitrust Bulletin** (1990), 1009.

- **Article 86 of the Treaty of Rome**

The second second pillar of EU competition policy, Article 86, prohibits abuses of a dominant position that may affect trade between EU Member States.

Where the U.S. took a structural approach to monopolization, focussing on dominance, **the EU approaches dominant structures more leniently**, focusing on the abuse side of the equation. Article 86 accepts the existence of dominant firms but asserts a power to control their conduct. The integration motive drives this difference. The EU accepts dominance so its companies can achieve the economies of scale unavailable when previously confined by national boundaries. But abusive conduct may be found illegal. Dominant companies may not use their power to distort competition in the common market.[119]

The level of dominance required to attract attention is also greater than in a fully integrated regime such as the U.S.. While the U.S. defines dominance as independence from the market, the EU allows *independence* but only so far as it is not used to appreciably *influence* the market.

For example, in *Continental Can*,[120] the EU Commission identified the hallmark of dominance as **overall** independence of behaviour on the market. In *United Brands*,[121] the European Court of Justice defined dominance as the ability "to behave to an appreciable extent independently of its competitors and customers and ultimately of consumers". Concerns arise when the dominant position is able to have an appreciable influence on the conditions under which that competition will develop.[122]

While dominance is less suspect in the EU, it is not tolerated to the exclusion of small businesses. They are protected not only for traditional equity

[119]*NV Nederlansche Banden-Industrie Michelin* v. *Commission*, **European Union Review** (1983), 3511.

[120]*Continental Can*, **European Union Review** (1973), 215.

[121]*United Brands*, **European Union Review** (1978), 207.

[122]*Hoffman-La Roche v. Commission*, **European Union Review** (1979), 520.

reasons,[123] but also for integrationist reasons. The presence of small business checks the kind of behaviour to which dominant companies in Europe may be prone: the re-imposition of divisions along Member State lines.[124]

- **Affecting trade between Member States**

The integration criterion present in both competition articles described above has been expanded through an ever-lowering of the jurisdictional hurdle defining what activity may be subject to EU-wide competition rules.

The reduction began soon after the formation of the Communities. In 1966, the *Consten* court explained that what is particularly important is whether the agreement is *capable* of constituting a threat, *either direct or indirect, actual or potential*, to freedom of trade between Member States in a manner which *might* harm the attainment of the objectives of a single market between States.[125]

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[123]De Jong, "Anti-trust and International Competitiveness: The European Experience", **Antitrust Law & Economics Review** (1988), 53:

> Fairness is important in the thinking of the European Union; the Commission has consistently expressed for the past 20 years...that the viability of small business is important and should be taken care of.

Walsh and Paxton, *Competition Policy: European and International Trends and Practices*, London: Macmillan, 1975, p. 2:

> "Bigness" has been preached as an economic gospel for most of the post-war years...but the social problems of large concentrations of industry are beginning to be recognized. There is an increasing awareness...within the EEU, that there is a place for the small neighbourhood firm and that sometimes the economies of scale tend to dehumanize men's working environment.

[124]Kalmansohn, "Application of EEU Articles 85 and 86 to Foreign Multinationals", 2 **Legal Issues of European Integration,** (1) (1984), 6:

> the EEU has actively supported the existence and viability of small and medium size enterprises within the Community...the EEU envisions that they can serve as an effective counterweight to large common market-wide enterprises, which are prone to partition and "isolate" markets along national lines, contrary to the goal of integration.

[125]*Consten and Grundig v. Commission*, **European Union Review** (1966), 341. A few years later, the Court in *Miller International Schallplatten GmbH v. Commission*, **European Union Review** (1978), 131, confirmed that the Commission did not have to prove that an agreement actually affected trade, just that it was capable of doing so.

In the *BNIC* cases, the court extended the notion of capability, indirectness and potential for harm even further.[126] Price-fixing of a raw material, that itself did not cross a border, satisfied the inter-State trade requirement if the material were in a production process that was done in another State. In *Re Fire Insurance*, an agreement solely within Germany was found capable of affecting trade because one party had branches in other States.[127] In *Tepea*, the Court indicated that it would prohibit all agreements designed to partition a national market internally.[128] *Intra*-State partitioning satisfied the requirement of *inter*-State partitioning because it tended to divide the Community along national lines.[129]

As a result, very little evidence needs to be adduced by the Commission to satisfy the effect on the inter-State trade requirement. The integration process itself combines with the Court's work here to create a symbiotic and self-fulfilling circle. As barriers fall within the Community, most agreements of any commercial significance will satisfy the inter-State threshold.[130]

- **Integration and the rule of reason**

The integrationist movement has also created a different rule of reason than that which developed in an integrated regime.

The different structure of EU competition law creates less of a need for a rule of reason to develop. Moreover, one difference exists in the very structure of the competition law of the EU. As mentioned above, the EU, unlike the U.S., contains a specific exception from its prohibition: Article 85(3). This has

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[126]*Bureau National Interprofessionel du Cognac (BNIC) v. Guy Clair*, **European Union Review** (1985), 391; and *BNIC v. Aubert*, **European Union Review** (1987), 4789.

[127]Comm. Dec. OJ (1985) L 35/20 upheld by the EUJ in *Verband der Sachversicherer*, **European Union Review** (1987), 405 (discussed by Wyatt & Dashwood, *op.cit.*, p. 393).

[128]*Tepea B.V. v. Commission*, **European Union Review** (1978), 139.

[129]See also *Brasserie de Haecht v. Wilkin (No. I)*, **European Union Review** (1967), 407; and *Delimitis v. Henninger Brau*, **Common Market Law Review** (5) (1992), 210.

[130]Weatherill & Beaumont, *op.cit.*, p. 612.

reduced the pressure that would normally have been exerted upon the *per se* prohibition itself.

The 85(3) criteria provide **the statutory possibility for a tolerance of cartel agreements that goes beyond what U.S. courts would permit even under the rule of reason.** The explicit exemption provision makes the introduction of an implicit justification procedure under a rule of reason less necessary. The Sherman Act, by contrast, contains no explicit exemption.[131]

Still, a form of rule of reason has developed judicially. The Court of Justice has deemed that:

- To determine the application of article 85 (1), the court needs to consider if, as a reasonably foreseeable consequence of an agreement and in light of the legal and non-legal factors, the agreement might produce a noticeable effect on the trade between Member States.

An examination of the economic realities of competition is required.[132]

Despite never delineating these extra factors by the term "rule of reason",[133] the European Court of Justice has allowed them to work in the case law in three ways.[134] The example that best evinces the integrationist movement within the EU rule of reason is that of "indispensable inducement", which states that **but for** the restriction on competition, there would be no competitors in the first place, and no competition to restrict.

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[131]See Weatherill, *op.cit.*, p. 625; Korah, *op.cit.*, pp. 1014-5; Timberg, *op.cit.*, p. 137.

[132]Malawer, "International Law, European Community Law and the Rule of Reason", 8 **Journal of World Trade Law** (17) (1974), 21.

[133]Whish and Sufrin, "Article 85 and the Rule of Reason", 7 **Yearbook of European Law** 1 (1987), 29: It is interesting to note that the Court itself has never used the term "rule of reason" when considering Article 85(1) in its judgments, including those given since the arrival of Judge Joliet in 1985.

[134]These are: the primary one, also available in the U.S., concerning indispensable inducement; an ancillary restraints doctrine; and one allowing restrictions based on objective criteria that are applied non-discriminatorily. For an excellent description of the development of all three, please refer to Wyatt & Dashwood, *op.cit.*, pp. 406-8.

In *Technique Miniére*[135], the Court admitted that the object or effect of an exclusive dealing agreement could only be determined in its economic, and not merely legal, context and adopted the view that restrictions without which a transaction would not be viable do not, in themselves, restrict competition.

The *Nungesser* case added two integrationist factors, however. An exclusive dealing restriction could escape prohibition if it were true that without some protection against competition, no one might have been willing to take the risk of entering the market, especially of entering the market of **another Member State**. That is, the defence is especially available if the anticompetitive activity or restraint is necessary to link formerly separate markets. The concern with integration qualifies the rule of reason in this important respect.

The U.S. courts in *Sylvania* allowed absolute territorial restrictions because without them others would free-ride on the new entrant's efforts.[136] The EU has not gone this far.[137] The *Nungesser* court stated that absolute territorial protection was too much and, thus, remained consistent with its original prohibition of absolute territorial restraints in *Consten.* The problem for Europe is not in the **exclusivity** of the restraints, but in their **territoriality**.

The most that can be expected to develop, therefore, is a *sui generis* EU rule of reason that accommodates, *inter alia*, the objective of market integration.

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[135]*Société Technique Miniére v. Maschinenbau Ulm*, 5 **Common Market Law Review** (1966), 357.

[136]See also Sharma, Thomson and Christie, *op.cit.*, 1994.

[137]B. Hawk, *op.cit.*, pp. 74-5:
EEU law stands in stark contrast. There has always been and continues to be a *per se* -like rule with respect to absolute territorial restrictions along member state boundaries... One should not expect that the prevailing economic doctrine in the U.S. will bring about a volte face in U.S. case law. The free rider rationale does not have the same influence in the EEU, at least where parallel imports are concerned.

Whish, *op.cit.*, p. 29:
some cases contain a hint of a partial rule of reason, but subject to the overriding issue of market integration... If there is a rule of reason in EEU law, it is of limited application, for it is displaced where an agreement has the effect of retarding the integration of the common market.

6.5 Possibilities for harmonization

It might be reasonable to assume that, as Europe integrates, the competition policies of other integrated markets such as the U.S. will become more applicable. Despite virulent debate on the subject,[138] the sensible conclusion is that they will not. As the markets are different,[139] so too are the policies applicable to them.[140] **Equity and integration have more play in the EU.** In fact, as the U.S. has become more concerned with efficiency, it has narrowed its focus and strayed somewhat further from the equity root of antitrust. The U.S. may be becoming less rather than more relevant to the EU, although more recent critical re-evaluation of Chicago School anti-structuralism does suggest some possible shift back towards equity-based origins in the U.S. (see section 4.2.3 above).

The EU cannot afford to look only across the Atlantic. It maintains wider socio-political considerations within its laws. Indeed, it must maintain at all times its multi-leveled focus on efficiency, equity and integration, if its project is not to be subverted by individualistic profit-taking. Profit maximization is thus kept within strict bounds in Europe and only unleashed as it will serve to integrate the communities.

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[138]B. Hawk, *op.cit.*, p. 53:
The U.S. Chicagoan "revolution" has generated criticism of EEU competition law as outmoded and insufficiently reflective of the "new economic learning" in the U.S....appeals for a "rule of reason" under Article 85(1) frequently cite the trend away from *per se* rules in the U.S. towards the rule of reason.

Van Bael, p. 12:
Nobody denounces the enthusiasm with which the Commission and the Court pursue their goal in their respective activities. However, in the field of territorial restrictions there are instances where, in terms of consumer welfare, it would pay to adopt a 'rule of reason' instead of the *per se* approach hitherto followed.

[139]B. Hawk, *op.cit.*, p. 54, who notes the still existing "markedly contrasting economic realities where the EEU faces language and cultural differences, multiple currencies, shifting exchange rates, etc.".

[140]B. Hawk, *op.cit.*, p. 85:
the American revolution, at least in its most extreme form, will not be repeated in the EEU because of the policy and statutory differences between U.S. and EEU law.

7. Competition Philosophy Spectrum in the Triad

U.S. citizens have far more individualistic attitudes and are more willing to challenge experts and resist officialdom. This has its advantages, but it does cause much inaction and indecisiveness that foreigners point to as instances of inefficiency.[141]

When a country has been governed by a close-knit group of politicians and civil servants working in collaboration with business and labour groups, they can reduce some of the uncertainty because of the mutual trust of their ongoing relationships. Some European countries over the past century, or Japan for the four decades from the 1950s to the 1980s, may be cases in point.[142]

This Paper has placed competition philosophy on a spectrum ranging from individualism to communitarianism. Models depicting these philosophical positions were presented in sections 2 and 3. In sections 4, 5 and 6 we presented the evolution of competition policy thinking and laws in a historical context in the U.S., Japan and the EU. Where would we locate the four jurisdictions on the competition philosophy spectrum?

Much as a pure market economy does not exist, none of the jurisdictions examined in this Paper would correspond to the theoretical extreme positions of pure individualism or pure communitarianism. Each is characterized by a mix of competition philosophy features.

In comparing the **substantive competition laws** and **enforcement practices** among the Triad countries, we submit that:

- U.S. competition policy, with regard to both substantive standards and enforcement, is closest to the individualistic end on the competition philosophy spectrum;
- Japan's competition policy, with regard to both substantive standards and enforcement, is closer to the communitarian point on the spectrum; and

[141] Avinash K. Dixit, **The Making of Economic Policy**, Munich Lectures, MIT Press: Cambridge, MA, (forthcoming) 1996: 109.

[142] Avinash K. Dixit, **The Making of Economic Policy**, Munich Lectures, MIT Press: Cambridge, MA, (forthcoming) 1996: 54.

- the EU competition policy, with regard to both substantive standards and enforcement, is located not very far from the Japanese communitarian position.

We now turn to develop these conclusions by comparing the similarities and differences in the Triad with regard to:

(a) specific **characteristics** of competition policies, such as:

- criminal vs. civil treatment,
- the development of the rule of reason vs. the *per se* standard,
- the interplay of public interest, integration and economic efficiency considerations,
- economic efficiency, producer and consumer welfare, and
- corporate governance issues, such as relationship-based networks.

(b) competition **law jurisprudence and enforcement** relating to major anti-competitive business practices, such as:

- conspiracy,
- abuse of dominant position/firm size,
- mergers,
- vertical arrangements, and
- enforcement of competition laws in practice.

7.1 A comparison of characteristics

● Criminal vs. civil law treatment

The criminal vs. civil process dichotomy has an impact on the eventual legal outcome, since the standard of proof to be met by the prosecution in criminal cases is substantially higher than that placed on the plaintiff/applicant in civil litigation.

Among the four Triad jurisdictions, there is not much formal statutory difference in competition law with regard to the criminal and civil dichotomy.

There are, however, certain significant differences with regards to the practice, as we discuss below in sub-section 8.2.

- **The rule of reason vs. the *per se* standard**

The U.S. has developed a relatively strong rule of reason because it exalts the role of the individual. Europe and Japan place less value on developing such a rule, because they place less value on litigation and the judicial development of the law. In the development of an antitrust rule of reason, Europe and Japan share more similarities with each other than with the U.S.. As a result, the rule of reason approach that evolved in Europe and Japan is less well developed than that found in the U.S..

- **Public interest and integration**

- **Public interest.** In **Japan**, the Fair Trade Commission or the courts have to decide whether an unreasonable restraint of trade, such as a cartel, is contrary to the public interest.[143]

EU: The *Treaty of Rome* reminds the European Commission to remain in-tune with the aims of economic and social cohesion in Europe, and other fundamental objectives of the *Treaty*. Accordingly, public interest considerations have led the European Commission to take a sympathetic view of certain state subsidies by Member State governments. The Commission acknowledges that state assistance may distort trade among member states by the misallocation of resources but argues that state subsidies may ease the social problems associated with structural change. However, in authorising state aid, the Commission often attaches conditions that have the aim of mitigating negative effects on competition. Exemptions for state subsidies are justified on the grounds that competition may not ensure that the most efficient firms will remain in the market or may entail unacceptably high social costs.

- **Integration.** The integration motive is not an element in U.S. or Japanese competition policy, but is central to competition policy in the EU. The use of

[143]Mitsuo Matsushita, ***International Trade and Competition Law in Japan***, New York: Oxford University Press, 1993, p. 90.

competition policy as an instrument for integration has resulted in some rules in the EU that compromise the market efficiency approach for the sake of longer-term market integration and efficiency.

- **Economic efficiency, producer and consumer welfare**

U.S.: The interpretation of efficiency in the U.S. appears to depend largely on assessing benefits obtained by consumers. In other words, the consideration of economic efficiency is narrowly focussed to imply consumer welfare or "consumer surplus".

EU: Although efficiency considerations take a back seat to integration, EU competition legislation provides for well-articulated considerations of both consumer and producer interests. For example, the 1990 *Merger Regulation* includes considerations of consumers' advantages or interests as well as the market position of firms.

Japan: What economic efficiency emphasizes in Japan has been a matter of considerable debate. Depending on circumstances, the networks such as the *keiretsu* setup can reduce transactions cost and enhance efficiency. We will return to this point below in sub-section 7.3.

- **Corporate governance: relationship-based networks**

- **Relationships.** European competition policy deals with a heterogeneous market of both individualistic actors, and those, as in Germany, who also factor broader relationships into their corporate decisions. The competition policy that has developed seeks to channel both the profit maximization motive, and the motive that seeks relationships, into a uniquely European competition policy that assists in relationship-building between Member State markets.

Japanese anti-monopoly law has developed to deal with a communitarian market based on long-term relationships. Many Japanese industrial practices and relationships with government seem to Europeans to be somewhat extreme examples of nonetheless familiar practices, rather than the U.S. perception that they are designed perfidiously to deny foreigners access to markets in Japan.

- **Corporate governance.** Some continental European and Japanese similarities in corporate governance run as follows. The Germans have bank-centred industrial groupings and sympathetic officials in the economics and technology ministries. French industry is used to administrative guidance provided through networks based on the Ecole Nationale d'Administration. Germany is the land of cartels and Italy the land of personalized managerial networks. In many European countries, antitrust implementation has been either modest or *industrie-freundlich.* Given this background, European officials tend to be more sympathetic to Japanese administrative arrangements.[144]

Thus, whereas individualistic considerations propel corporate governance in the U.S., communitarian factors drive the policies of business and government in Japan and continental Europe.

7.2 Competition law and jurisprudence

● Conspiracy and export cartels

• Conspiracy

U.S.: The prohibition of agreements among competitors has long been viewed as an offence in the U.S.. The development of the concept of a *per se* offence is a manifestation of the strong philosophical aversion to collusion that leads directly to monopolistic pricing and practices with no offsetting gains. However, in permitting an efficiency defence the U.S. Supreme Court in a 1979 case may have eroded the strong *per se* treatment of the proscribed collusive conduct.[145]

EU: Let us begin with some historical examples. In Germany, at the turn of the century, the legality of cartels and other restraints of competition were generally governed by the *Civil Code* of 1900. In general, the courts were reluctant to restrain the activities of cartels and monopolies. Even the *Cartel Ordinance* of 1923 did not make cartels illegal *per se*; cartels were legal in

[144]Wilks, *op.cit.*, p. 40.

[145]*Broadcast Music, Inc., v. Columbia Broadcasting System*, 44 US 1 (1979).

principle. It was not until 1949 that changes were introduced, when the Allied authorities under the *Occupation Statute* introduced the Decartelization and Industrial Deconcentration Group laws in Germany.[146] In Sweden, cartels were legal until 1993. Many industries in Sweden are highly concentrated and have been characterized by cartel agreements. Often these cartel agreements were politically sanctioned and supported by regulation.[147]

The evolution of the philosophical approach to horizontal agreements or collusion in the EU has involved the balancing of the merits and demerits of competition and cooperation. Price-fixing and market-sharing arrangements have been firmly dealt with by the European Commission. For intra-EU cartels and foreign cartels aimed at the EU, the treatment has been near to a *per se* prohibition. However, the Commission is sensitive, within certain limits, to cooperative agreement between firms. That the Commission can view state aids and cooperation as competition reinforcing practices is reflected in its generous definition of small and medium enterprises (SMEs)[148] for the purposes of granting SMEs block exemptions under competition law for specialization and R&D agreements.[149] Horizontal agreements within national boundaries are prohibited, although they receive more lenient treatment when between competitors from different Member States.

Japan: In principle, the Japanese competition law, the AML, prohibits cartels aimed at anti-competitive practices such as fixing or raising prices, restricting production or segmenting markets. To control anti-competitive collusion, which can easily be facilitated by trade associations, the AML prohibits the anti-competitive activities of trade associations in Japan.

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[146]Kurt Stockmannn, "Lessons from other Countries: The Federal Republic of Germany", in R.S. Khemani and W.T. Stanbury, eds., *op.cit.*, 1991 (vol. I), pp. 613-36.

[147]Stefan Fölster and Sam Peltzman, "The Social Cost of Regulation and Lack of Competition in Sweden", in Richard B. Freeman and Robert Topel, eds., ***Reforming the Welfare State: The Swedish Model in Transition***, Chicago: University of Chicago Press, 1996 (forthcoming).

[148]For instance, two firms with a 20% combined share of the whole EU market would still qualify as SMEs.

[149]Ken George and Alexis Jacquemin, "Competition Policy in the European Community", in W.S. Comanor, K. George, A. Jacquemin, F. Jenny, E. Kantzenbach, J.A. Ordover and L. Waverman, eds., *op. cit.*, 1990: 206-45, p. 212.

Nonetheless, cartels in Japan are authorized, not on account of competition considerations, but due to other policy goals. For example, the MITI has used administrative guidelines to achieve horizontal agreements or the grouping of firms to promote the protection of small firms, to assist depressed industries and to promote basic R&D.

Export cartels. Export cartels permit the shifting of profits from foreigners to home-country firms, presumably on grounds that no national is injured and that domestic producers profit. All the Triad countries have laws or policies that permit export cartels to operate from within its borders. Export cartels are authorized by governments or are broadly exempted from competition law.[150]

Overall, competition law and philosophy in the Triad with regards to conspiracy and cartel practices began with a position of prohibition. To a large extent, the U.S. stands out for its strong *per se* treatment, while the EU provide near *per se* standards, and Japan tends to dilute its proscription of cartels and horizontal collusion by granting exemptions and recourse to administrative guidance exceptions.

- **Abuse of dominant position/firm size**

U.S.: Monopolization, while central to its anti-trust regime, has been treated in the U.S. through the rule of reason. During the 1940s-1960s, the structuralist approach sustained the systematic break-up of concentrated industries without regard to efficiency issues. In the structuralist view, the threat of entry into concentrated markets was thought not to pose an effective check on the exercise of market power. The so-called Chicago School proponents, during the 1970-1980s, argued that the danger of successful monopolization or exploitation of market power was fairly low. Thus, in the mid 1980s, high market concentration or even dominance by itself did not figure prominently in initiating competition policy action in the U.S..

[150]See William Ehrlich and I. Prakash Sharma, "Competition Policy Convergence: The Case of Export Cartels", **Policy Staff Paper** No. 94/03, Ottawa: Foreign Affairs and International Trade, April 1994.

However, in the post-Chicago School period, some business practices, such as first mover advantages or differences in information between an incumbent and potential entrants or the reputation of the incumbent, were argued to pose barriers to entry and to contribute in maintaining a dominant position. If the Microsoft case is any indication, U.S. antitrust policy with regard to abuse of dominance may be moving back in the direction of a most aggressive position on competition philosophy spectrum.

EU: The abuse of a dominant position in the EU is condemned but not the existence of a dominant position. In other words, a dominant firm will be tolerated so long as it does not take advantage of its position and engage in uncompetitive behaviour. In general, like the U.S., the abuse of dominance in the EU is examined by the rule of reason standard, which considers the background of the circumstances of each case. There is no provision for the dissolution of existing concentrations in EU law, instead, abuses are prohibited.

Japan: The AML recognizes that a powerful enterprise can become a monopoly by excluding or controlling the business activities of other firms and can stifle market competition. Two main elements of monopolization are exclusion and control in the marketplace. In principle, the AML provides for both structural and behavioural controls of monopolization in Japan. Deconcentration measures such as a break-up of an existing enterprise became theoretically possible when the *per se* structural control of monopolistic situations was hesitatingly revived in 1977.

In summary, the U.S. stands out among the Triad by giving centre spot to firm size or market shares, i.e. **structural** and quantitative elements, in determining a monopoly problem. In contrast, Canada, the EU and Japan appear more to focus on the abuse of monopolistic **behaviour** than the bigness or firm structure itself. The U.S. also allows for an effective dissolution power to deal with existing monopolies, which is not done explicitly in either Japan or the EU.

On balance, the emphasis in U.S. competition policy on structural elements such as large firm size reflects the philosophy that firms with large market share are likely to limit individualistic freedoms and harm consumer welfare. Although both the EU and Japan also apply market share to test for monopolistic positions, the questions asked there are whether a monopoly abused

its powerful position and harmed the public. On the other hand, the treatment of abuse of dominance in the EU and Japan is consistent with their communitarian perspective to allow firms to become large-sized provided society derives offsetting benefits.

First, the U.S does not require an explicit market share test to determine dominance. Second, competition policy in the EU and Japan, concerns itself largely with anti-competitive behaviour rather than structural issues. Third, in the U.S. it is possible to break-up existing dominant firms. Such a provision does not exist in the EU and is nearly impossible in Japan.

- **Mergers**

U.S.: Mergers in the U.S. are assessed in terms of their (anticipated) effect on consumer welfare as measured by the impact on consumer prices. This impact is determined by examining market power. In U.S. jurisprudence and in the *Merger Guidelines* of 1992, market power has been examined by looking at such quantifiable market share and structure data and indices as Herfindahl-Hirschman (a measure of market concentration). Potential efficiency gains of a merger may be considered but traditionally have not figured prominently. In other words, no absolute efficiency defence exists in the U.S..

A pre-merger notification to both the Federal Trade Commission and the DOJ is required for most mergers above US$ 10 millon threshold levels.[151] Decrees or orders may require divestiture of lines of business that are the basis for the anticompetitive concern. Non-structural remedies also exist. In contrast to the EU, Canada or Japan, the U.S. statutory scheme explicitly allows private parties to sue for and have injunctive relief against "threatened loss or damage" arising from a violation of section 7 of the Clayton Act. The Department of Justice (DOJ) has tended not to view vertical mergers with concern and its approach appears more lenient than U.S. jurisprudence.

[151]Reportable mergers in the U.S. would include transactions such as when one party has total assets or net annual sales of US$100 million or more and the other party has total assets or net annual sales of US$10 million or more; or when the buyer is acquiring 50% or more of the issuer's voting stock, even if the value of voting securities is worth US$15 million or less.

EU: Until the *Merger Regulation* of 1990, the power to control the emergence of dominant positions was largely absent in the EU. A merger has an EU dimension where: (a) aggregate worldwide turnover of all the firms concerned exceeds ECU5 billion; and (b) the aggregate EU-wide turnover of at least two of the firms concerned is more than ECU250 million. As in the U.S. and Canada, there is a pre-merger notification requirement in the EU.

Mergers that create or strengthen a dominant position and significantly impede competition in the EU are prohibited. In examining merger cases, the Commission considers factors such as: market structure; actual and potential competition from firms located both within and outside the EU; the market position, and economic and financial power of the firms; the opportunities available to suppliers and users; access to supplies and markets; barriers to entry; supply and demand trends for the relevant goods and services; the interests of consumers; and the development of technical and economic progress, provided that it is to the consumer's advantage and does not form an obstacle to competition.

The philosophy behind the control of mergers in the EU appears to be that mergers between firms with "small market shares" are unlikely to impede competition. Unlike Canada, the EU does not have an explicit efficiency defence in merger cases. Overall, however, merger control in the EU follows the rule of reason approach, which is also the case in the U.S..

Japan: Mergers that substantially restrain competition or are carried out through an unfair business practice are illegal. As in all other Triad jurisdictions, there is pre-merger filing requirement with the Japanese Fair Trade Commission (JFTC). In the *Yawata-Fuji* case, which was settled by a consent decision, the JFTC did not even consider whether efficiency issues would be relevant in the case.[152] Unlike the U.S., but as in the EU, there is no efficiency defence in Japan when large parties merge. In theory, JFTC can issue, as a measure of last resort, an order to break-up or split a monopolistic situation in Japan. However, in practice such deconcentration measures are nearly impossible to implement.

[152]JFTC Decision, 30 Oct. 1970, *Shinketsushū*, 16 (1970).

A considerable reliance in Japan, as in the U.S., is placed on quantitative tests for notification of mergers. The threshold tests, among others, include: (a) the market share of one company or the total share of two merging firms is 25% or more, or in the case of the three merging companies the total market share is 50% or more; (b) one or both merging firms rank at the top and occupy a 15% market share; or (c) the total assets of one the merging companies is above ¥10 billion and those of the other company is ¥1 billion, or (d) there is a small number of competitors in the merging firm's market. As for the investigation criteria, the JFTC considers economic or qualitative factors such as the conditions of competition in the relevant and the related markets in horizontal mergers and the degree of foreclosure of the market in vertical mergers.[153]

In summary, common to all in the Triad is the pre-merger notification requirement and the rule of reason civil control of mergers. However, the threshold levels beyond which a merger case becomes a reviewable matter is the lowest in the U.S. among the Triad, while the levels in the EU and Japan are quite high.

The U.S. competition philosophy with regard to the use of low threshold levels reflects that even "small-sized" transactions leading to business consolidation could compromise individualistic freedoms, economic efficiency and competition in the marketplace. Moreover, in emphasizing quantifiable over qualitative elements in examing specific merger cases, the U.S. allows less play for other factors that could possibly balance the negative effects of a small-sized merger. The reliance on quantitative factors in Japanese competition law, such as market shares and concentration indices, in assessing the anti-competitive potential in Japan of a proposed merger appears to reflect elements of U.S. competition law. However, Japan has a higher threshold for reportable cases. Neither Japan nor the U.S. nor the EU provides for an explicit efficiency defence. On the other hand, in the EU considerations of public interest and the integration motive provide some room for counterbalancing mergers that might be found objectionable on efficiency grounds.

- **Vertical arrangements**

[153]Mitsuo Matsushita, *op. cit.*, 1993, pp. 130-1.

Vertical relationships subject to competition law prohibition include: resale price maintenance (RPM), exclusive territorial and customer restrictions (ETCR), exclusive dealing (ED), tied sales (TS) and vertical franchising agreements (FA). Except RPM, all other vertical arrangements are basically examined under the rule of reason approach in the Triad. Such a convergence in the treatment of vertical arrangements reflects the philosophy in the Triad that vertical contracts can, depending on circumstances, both improve market competition and economic welfare or reduce competition and welfare in the economy.

All the Triad jurisdictions provide for a *per se* prohibition of RPM business arrangements. The philosophy behind the RPM illegality is the apprehension that RPM would facilitate horizontal price fixing or cartelization in the Triad.

In sum, all Triad jurisdictions treat vertical arrangements, except RPM, on a case-by-case basis, i.e., the rule of reason standard. Again, the U.S. is the only country among the Triad that still retains some echo of *per se* illegality/tests for exclusive dealing and, considerably less so, for tied sales business practices. Thus, the philosophy with regard to vertical restraints, the differences are not particularly striking, although with the U.S. set moderately apart.

- **Enforcement in practice**

Whereas enforcement in the U.S. and the EU regularly feature criminal prosecutions and penalties for competition law violations, in Japan the JFTC pursues primarily a civil-administrative process. Although criminal prosecution may be utilized for private monopolization and unreasonable restraints of trade, the agency appears to regard criminal indictment as a method of last resort.[154]

U.S.: In addition to federal authorities, the enforcement system in the U.S. also has other points of entry for state attorneys general and private parties. The ethics of democratic rights and individualistic profit motivate individuals to come to court and even potentially to amend the common law. The profit

[154]With regard to this issue, see Sharma, Thomson and Christie, *op.cit.*, 1994.

maximization motivation is that much stronger in U.S. case law, due to the incentives of treble damages and contingency fees, both only available in the U.S..[155] Thus, anti-trust compliance costs for doing business in the U.S. tend to be higher and the multi-faceted enforcement system fills business with greater uncertainty. As a result, some beneficial and pro-competitive mergers or business arrangements may fail to take place under the U.S. enforcement system.

EU: The EU follows an administrative approach to the enforcement of competition law. The European Commission Directorate-General for competition policy, DG-IV, has extensive powers to investigate, to prosecute and to impose penalties on offending parties.

The Commission's attitude is strongly influenced by integrationist concers. Horizontal cartels will be tolerated in cases where their market share is unimportant and there is no effect on inter-State trade. The Commission has ruled that trademarks, licensing agreements and copyright law may not be used to stop parallel imports.

With respect to the control of monopolization, the focus is behavioural, on abuse. The controls applied to monopoly problems are conduct remedies, which aim to control aspects of firms' behaviour. Some writers have argued that controlling the behaviour of dominant firms without some form of structural remedy, such as powers of dissolution, has not been particularly effective in the EU.[156]

Merger enforcement is administered and reviewed by a special Task Force within the DG-IV. The final authority in all competition cases rests with the European Commission as a whole. At stage one, the DG-IV routinely consults with the Directorate-General for Industrial Affairs (DG-III). At the second stage, the case is referred to the Advisory Committee of Member State Representatives. In the final round, the case comes before a corporate decision-making body of all the EU Commissioners. Some commentators have argued

[155]See Jorde and Teece, "Innovation, Cooperation and Antitrust" in ***Antitrust, Innovation and Competitiveness***, Oxford University Press, 1992, pp. 56, 58.

[156]Ken George and Alexis Jacquemin, *op. cit.*, 1990, p. 233.

that the DG-IV's merger assessments are often prepared to dovetail with the decisions made by the Commission based on other grounds.[157]

Japan: In principle, horizontal agreements, such cartels, price-fixing or market segmentation among firms in Japan may be challenged under the AML. But firms in government-induced cartels can argue for an exemption on grounds that they were simply following government guidance. The position of the JFTC is that there is no exception to the prohibition of cartels even though a cartel is based on administrative guidance. In contrast, court decisions in Japan have allowed some cartels created under administrative guidance to be accorded an exception.

Although the Anti-Monopoly Law provides for merger controls, the provisions have not been used to the extent in the U.S.. Up to 1992, none of the merger cases in Japan had led to a prohibition.[158] In some cases, corporations have been able, with the support of MITI, to merge despite objections by Japan's Fair Trade Commission.

A discussion on the philosophy of enforcement. Japan and Europe share a more communitarian ethic of relationship-building and a civil law tradition.[159] They have developed a system where individuals are less likely to come to law, are less profit motivated to come to law, and, when they do, are less likely to have effect on the law. When fines are used, they are in the form of a surcharge.[160] Even when responding to U.S. pressure to raise the level of

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[157]D. Neven, R. Nuttal and Paul Seabright, *Merger in Daylight: The Economics and Politics of European Merger Control*, London: Centre for Economic Policy Research, 1993.

[158]Mitsuo Matsushita, *op. cit.*, 1993, p. 129.

[159]Note "Trustbusting in Japan: Cartels and Government-Business Cooperation", 94 **Harvard Law Review**, 1981, p. 1066:

> Japan had modelled its legal system on the German civil code system - a fact that complicated the application of the American-based AML.

[160]Iyori, *op.cit.*, p. 242:

> The influence of German and European thought continues to this day in Japan. The imposition of a surcharge to participants to a price cartel was modelled after the administrative fine systems in both the German and EU competition laws.

its surcharge or strengthen its antimonopoly enforcement, the Japanese, for example, still look to the EU model rather than the U.S..[161] Both continental Europe and Japan share a history of having a foreign (U.S.) individualistic antitrust applied to their markets, but also of modifying the individualistic form of enforcement to suit their markets.

Similarly in contrast to the U.S., neither the EU nor Japan permit private parties to take competition cases related to non-criminal matters directly to court, nor to seek treble damages even in criminal matters.

7.3 Competition philosophy and the success of corporate models

Competition policy is an integral part of overall economic policy. One major result that policymakers want to deliver to their population is good job and business opportunities, and high levels of living. Good competition and trade policies should support and contribute to job creation, business activity and consumer welfare in the economy.

Some policy analysts worry about frictions among national corporate systems and pose the question: what will happen in the marketplace when the "I" of America goes up against the more communitarian "Das Volk" of Germany or "Japan Inc."?[162] Thurow believes this conflict has already begun:

Wilks, *op.cit.*, p. 20 on the role played by guidelines:

> In Britain, guidelines are often regarded as an empty, face saving device, easily breached and often ignored. In Japan they are taken far more seriously...they fulfil almost the same role as precedent in case law... the EU tends to use guidelines precisely to interpret and elaborate case law.

[161]Wilk, *op.cit.*, p. 31: When the Japanese "cartel surcharge...was set at a modest 1.5% of...turnover... The U.S. advocated an increase to 10%".

Also:

> The JFTC has announced that it will facilitate private actions by publishing fuller information and providing full evidence to the court... Suit filing fees have been reduced...but it remains highly improbable that triple damages or class action suits will become allowable. MITI points out that since such provisions do not exist in Europe, there is no reason why they should in Japan.

[162]Lester C. Thurow, *Head to Head: The Coming Economic Battle Among Japan, Europe and America*, New York: Warner Books, 1992, p. 125.

> ...a competition between two different forms of capitalism is already under way... [the] individualistic... British-American form of capitalism is going to face off against the communitarian German and Japanese variants of capitalism.[163]

Thurow and Blinder[164] place U.S. firms at the shorter-term, profit maximization end of the spectrum, with German firms closer to, and Japanese firms at, the communitarian end. Some commentators believe that communitarian corporatism is currently ahead of the individualistic approach. Each version has had its economic successes. However, Thurow emphasizes the strength, durability and flexibility of Japanese and German corporations.

In this Paper, the comparison of competition philosophies in the U.S., Europe and Japan suggests that the twin objective of sustaining good jobs and higher living levels can be addressed in two ways: the Anglo-American corporate competitive approach and the communitarian EU-Japan corporate governance approach.

7.3.1 Individualistic Anglo-American corporate governance

The Anglo-American corporate competition approach to competition policy places **the premium on achieving "efficient" market outcomes, at least over the short to medium term, and perhaps longer.** The quest for efficiency starts with producers competing in the marketplace and ends with lowest possible prices for consumers for quality products. How does the Anglo-American approach achieve its objectives?

First, the link from competitive efficiency to high living levels is quite direct. Low prices allow people to afford a bigger basket of goods and other things that matter to them in achieving high living levels. The standard of living of citizens increases as they experience expanding consumption opportunities.

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[163]Ibid.

[164]Alan Blinder, "Profit Maximization and International Competition", in **Finance and International Economy 5**, The AMEX Bank Review Prize Essays: In Memory of Robert Marjolin, edited by Richard O'Brien. New York: Oxford University Press, 1991. Mr. Blinder is currently a Vice Chairman of the Federal Reserve System in the United States.

Second, the connection between competitive efficiency and jobs is as follows. Competition among firms leads to an efficient use of resources. Companies are led to use management and production techniques that result in (a) lower costs, and (b) new products and varieties. Firms beat not only domestic but also international competition on account of their comparative price and quality advantages. The price and quality edge allows efficient firms to win orders and clients globally.

To hold on to and sharpen their price and quality advantages, firms engage in research and development to raise the productivity of their workers. Efficient firms can increase their market penetration and achieve higher sales and profitability. Competitive companies help policymakers meet the objective of expansion of business opportunities. Competition among efficient firms for skilled, knowledgeable and high productivity workers results in higher incomes. The objective of supporting and creating higher quality jobs is advanced by efficient companies.

In sum, the Anglo-American approach, by emphasizing efficient outcomes in a dynamic economy, promotes not only consumer welfare but also business opportunities and can support high productivity jobs. Business opportunities in the Anglo-American system expand as new entrants challenge incumbents by waging price and quality competition. Competition policy under the Anglo-American regime ensures that bigness and the restrictive business practices of corporations do not come in the way of the creation of businesses, high real-wage jobs and higher living levels.

7.3.2 Communitarian corporate governance

The EU-Japanese corporate governance approach promotes the development of efficient relationships by placing producers at the centre of competition policy concerns. How does the EU-Japan approach achieve its objectives?

Participants in the EU and Japanese markets, whether private or public, have an understanding of each other.

- First, the actors in European and Japanese markets understand, and place more value on, the importance of broader commercial relationships or networking.
- Second, their governments see more clearly the benefits of cooperation between businesses, and between businesses and themselves.
- Third, the relationships that develop are less embedded in contract law than those of an individualistic ethic.

Business philosophy in Japan and the EU has emphasized the importance of "live and let live" among competing companies. This is particularly true in recessions and for declining sectors. For example, in Japan the perceived benefits of lifetime employment promote the idea that corporations are worth preserving even when they suffer economic distress. The communitarian business ethic also justifies limiting opportunities for corporate takeovers by those who raise stock values at the expense of jobs. This thinking also justifies cross-ownership of Japanese corporations and suspicion of shareholder democracy. Nonetheless, the protection of traditional social institutions and avoiding markets that sort out winners and losers in bad times may protect jobs, but can also compromise economic efficiency and the reallocation of resources.

The emphasis on cooperative relationships in the corporate-government governance set-up is based on the expectation by the government that the corporate sector conducts its business affairs to ensure that jobs and business opportunities are available in the economy. The corporate sector, for its part, expects that the government will adopt regulations and policies that enable firms to maintain profitability and support jobs, now and in the future. So long as the EU-Japanese competition philosophy helps to achieve an overall satisfactory result, business practices may not be held to the first-best standards of economic efficiency. However, efficiency considerations cannot be entirely ignored. In this regard, and in a dynamic context, communitarianism can promote (although not inevitably) efficient corporations. Thus, the EU-Japan approach can achieve its objectives by directly creating an environment where longer-term corporate planning and growth is supported and high productivity jobs are sustained.

8. Conclusions

This Paper has attempted to offer an explanation and compilation of the differences in approach among the competition policies in the Triad that is at a deeper level than a comparison of the laws and case law in the four jurisdictions. It aims to look past the legal realm and into the cultural and philosophical ethics behind the markets. It has sought to understand better the urges behind the "anticompetitive" behaviour of market participants and so to understand better what forms of competition policy could be used to address the behaviour itself.

8.1 The convergence of competition philosophies in the Triad

The EU, Japan and the U.S. competition approaches, though based on different philosophical underpinnings, have been successful in historical perspective. Consequently, **one conclusion of this Paper is that there is no presumption that the "pre-dominant" form of competition policy in the world should be the U.S. version.**

Competition philosophies evolve in tandem with the progress a society makes. In the marketplace, firms not only compete globally but also sometimes cooperate with foreign-based firms. To tap the benefits of inter-firm cooperation in the pre-competition stage, national competition authorities are seeking ways to cooperate with foreign competition policymakers and enforcers. Thus, as a result of a convergence trend in corporate governance across firms in the same industry throughout the Triad, we see the Triad countries embarking on a fuller convergence curve with respect to competition approaches as well.

- **The U.S.**

The competition policy in the United States has developed considerably away from its original thrust of equity protection toward the consideration of market efficiencies. The equity root protects small businesses; the efficiency branch protects the consumer. Both are protected from action that seeks profit maximization to the exclusion of other goals. Nonetheless, U.S. antitrust remains grounded in the individualistic tradition. U.S. business and law are cold to communitarian concerns. This sets the U.S. apart from the competition

policies that have developed in Japan and continental Europe. Both Europe and Japan use administrative guidance as the first resort, fines as a last resort. The enforcement of U.S. competition policy is more "confrontational" and litigious.

Consider the evolution of competition policy in the U.S.. Over a century ago, the U.S. tackled the issue of the integration of its economy and focussed on economic development through competitive market structures, including by busting up dominant trusts and monopolies. In the 1970s and 1980s, the focus in the U.S. shifted from structuralism to efficiency considerations, and since then, more narrowly, to firm behaviour issues. The role of government regulation and intervention, especially in technologically advanced industries, has always been hotly debated in the U.S..

To succeed in a global information-based economy, large and small companies need to tap into global networks and meet global standards. World-class businesses need local communities that command good infrastructure, innovative thinkers, workers with superior production skills and international traders who sit at the crossroads of cultures and manage the intersections. To create and sustain world-class capabilities, communities need a way to bring people together to define the common good, create joint plans and identify strategies that benefit a wide range of people and organizations. Business leaders must understand how strong local communities can help them become more globally competitive.[165]

In this Paper, we have argued that U.S. corporations and law largely ignore communitarian concerns. In a knowledge-based economy, however, a profit maximizing agenda that leaves out social and community interests may not be optimal. Businesses derive advantages not only from creating company-specific resources but from establishing linkages outside the company in the community as well. This view is well captured by Peter Drucker:

> [I]ndividuals, and especially knowledge workers, need an additional sphere of social life, of personal relationships, and of contribution outside and beyond the job, outside and beyond the organization ... [E]very developed country needs an autonomous, self-governing social sector of community

[165]Rosabeth Moss Kanter, "Thriving Locally in the Global Economy", **Harvard Business Review** (September-October 1995), 151-60.

organizations—to provide the requisite community services, but above all to restore the bonds of community and a sense of active citizenship.[166]

By placing knowledge workers further along the spectrum toward communitarian concerns and activities, the U.S. corporate agenda could achieve higher productivity levels in a knowledge society. Such a realization would entail corporate governance in the U.S. evolving in the direction of the EU-Japan communitarian model.[167]

- **The EU**

In the EU, integration of the European market has been an overarching objective. The harmonization of government regulations and intervention in achieving this goal is accorded a significant role. Consequently, the communitarian markets in the EU are not driven by the U.S. style emphasis on economic efficiency. However, once the EU accomplishes economic integration, it is likely to shift from its relatively inward-looking market attitude to a wider, global marketplace perspective.

A fenced-in internal EU market may offer profit and job security to insiders over the short and medium term. It is hardly a sustainable scenario in the long run. The extent of market growth is limited by demand growth. Earlier in this century, an integrated and seemingly self-sufficient U.S. had coasted along by trading only a small proportion (7% to 9%) of its GDP. U.S. participation in the world economy since then has expanded considerably (to over 20% of its GDP in the early 1990s).

To spruce up corporate growth and profitability, EU corporations would have to scour markets outside the EU to score commercial success and source

[166]Peter F. Drucker, ***Post-Capitalist Society***, New York: Harper Business, 1993, pp. 173-8.

[167]Derber, "Individualism Runs Amok in the Marketplace", **Utne Reader** (111), 1944, p. 116:
...at Saturn, the General Motors subsidiary [and joint venture between GM and Toyota] in Springhill, Tennessee... Saturn vests employees with a version of lifetime employment and empowers workers to co-manage and share decision-making power from top to bottom of the company while also making an unequivocal commitment to quality, which gives employees a sense of responsibility to customers. Social economics is thus good for business.

new technology and knowledge. In a trade sensitive world, EU companies would find better market access and be able to establish better long-term relationships abroad if the Commission were willing to accord undistorted domestic access to non EU enterprises. For instance, the further opening of EU markets, such as the agricultural market, would require firms to achieve economic efficiencies to meet non EU competition. Consequently, in the future, competition policy in the EU is likely to incorporate more fully the economic calculus of the global marketplace.

- **Japan**

Historically, competition in Japan was less direct and less confrontational. U.S.-style confrontational competition resulted in demands for protection. Pro-cartel legislation was enacted in 1930s. Japanese cartels were an essential backbone of the Japanese government's military and political drives to build an empire in Asia. Before the Second World War, efficiency, consumer interests and competition issues did not figure in the calculus of economic nationalism and imperialism. The Anti-Monopoly Law of 1947, largely modelled after U.S. antitrust legislation, was amended in the early 1950s to tolerate cartels and the administrative guidance of specific industries by government ministries. The strength of Japanese corporate governance lay in cooperative long-term relationships. Consequently, Japan adapted the AML to a competition philosophy conducive to achieving the goal of rebuilding the economy from the ruins of the Second World War. Competition policy in Japan has accommodated the role of the government and regulation of the economy.

In Japan, industrial restructuring and political evolution are underway. Exposure to foreign countries has brought consumers in Japan the information that prices of many goods are cheaper overseas than in Japan. Japanese corporations are having to cope with the higher value of the yen and have started manufacturing and sourcing abroad. Over the last decade, Japanese foreign direct investment and trade have increasingly been with Asian countries. Considerations of economic efficiency are leading them to question the worth of institutions such as the practice of life-time employment and long-term relationships. Such a debate goes to the heart of the *keiretsu*—Japan's corporate governance system.

In this Paper, we have argued that long-term relationships are the hallmark of Japanese business arrangements and have served the country well on balance. Nonetheless, the functioning of the *keiretsu* system currently violates an important principle of international commerce—the principle of **transparency**. Competition policy in Japan has to come to grips with this serious inadequacy. But Japan is changing. The attitude toward competition policy is also evolving from the needs of a "shortage economy" to an advanced country in pursuit of technological innovations, higher productivity and higher living levels.

8.2 Final reflections

In the medium term, competition policy in the Triad countries is likely to face fairly similar challenges of corporate and economic restructuring, as well as issues related to the information age and the emergence of a knowledge-based economy. As the pace of transactions zipping across national borders picks up and firms adopt similar business management practices, competition policy becomes a candidate for some form of coordination among industrialized countries.

During the 1950s to 1970s, the European countries and Japan were catching up to advanced U.S. industries. The role of activist government industrial policy in Europe and Japan was at variance with the view in the U.S.. But since then, the Triad countries appear to be converging to the view that direct government production and involvement in the science and technology sector does not translate into durable commercial success.[168] In the past, governments in Europe and Japan could subsidize domestic firms to reach a target, which they could set relative to what U.S. industries had already achieved. When competitors are running neck and neck, such targetting and

[168]For example, Article 130 of the Maastricht Treaty states that a system of open and competitive markets is required to make EU industry competitive. Furthermore, it warns that the title of industrial policy in the EU:

> shall not provide a basis for the introduction by the Community of any measure which could lead to a distortion of competition.

See also Sylvia Ostry and Richard R. Nelson, **Techno-Nationalism and Techno-Globalism, Conflict and Cooperation**, Washington, D.C.: The Brookings Institute, 1995, p. 61.

picking of winners is a hazardous game. Firms have to take on the market competition; bureaucrats cannot do it for them.

Countries with advanced economic sectors such as Japan, the U.S., the EU and Canada confront the issue of raising productivity through research and development, innovations and the production of new knowledge. There is a vigorous debate on whether large-sized companies or concentrated markets provide the best milieu and spurs to achieve these objectives. The current thinking is that competition can help foster efficient and innovative firms that need not necessarily be large in size.[169]

A deepening of the thinking in the Triad countries that most business transactions have to go through the market system rather than the regulatory and government guidance system would broaden the scope for the application of competition policy. In sum, we see a widening and deepening of cooperation among the competition authorities in the Triad countries on investigating violations and the enforcement of national competition laws.

The international trading system would benefit from a better understanding among the Triad countries of how best to respond to these issues in a symmetrical and coordinated manner. Recognizing, understanding and respecting the key motivations behind the differences between the Triad are essential steps to avoiding conflict and to developing a coordinated and globally effective competition policy.

Also critical is understanding that none of the Triad has the "best" or "ideal" competition policy. For example, the failure of the Japanese system to address adequately the lack of transparency in *keiretsu* corporate governance is serious. But the litigious and confrontational nature of the U.S. legal system (including antitrust law with treble damages, contingency fees and multiple entry points for litigation) makes many observers uneasy and arguably chills legitimate market activity. Moreover, all the "major" systems include questionable sectoral

[169] See I. Prakash Sharma, "Optimal Patent Term and Trade: Some Considerations on the Road Ahead", **Policy Staff Paper**, No. 93/12, Ottawa: Department of Foreign Affairs and International Trade, October 1993, pp. 64-5.

and other exemptions, while the use of the *per se* rule is arguably too pervasive, in the the U.S. even somewhat more than elsewhere.[170]

As international cooperation on competition enforcement expands and the debate on the convergence and compatibility of standards or guidelines is more directly engaged, we must continue to guide ourselves by what makes sense in practice in the marketplace and with regard to the marketplace's capacity to produce better quality jobs and higher living standards. The specific instruments found in competition arsenals are simply tools to be used to achieve those goals, not ends in themselves.

With regard to these issues, see Sharma, Thomson and Christie, *op.cit.*, 1994.

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