UNCTAD IGE

CUTS CONTRIBUTION TO ROUNDTABLE:

(c) <u>Cross-border anti-competitive practices: The challenges for developing countries and economies in transition</u>

The idea that cross-border anti-competitive practices can seriously restrict trade and should, therefore, be addressed within a multilateral context is not new. The Havana Charter of 1947 envisaged that the proposed International Trade Organisation (which was not formed and instead the General Agreement on Tariffs and Trade was initiated in 1947, the precursor to the WTO) would have power to prevent restrictive business practices that restrain competition and affect gains from trade. However, the Havana Charter did not succeed. Although the momentum led to the adoption of "The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices" also referred to as the UN Set of Principles And Rules on Competition by UNCTAD in 1980.

In January, 1997 the WTO established a working group on the interaction between trade and competition policy to explore the linkages and see whether a multilateral agreement on competition can be incorporated in the WTO acquis. The idea was carried forward in the Doha Development Agenda. However, same was taken off the negotiating agenda in 2004 due to opposition by developing countries to negotiations on several issues, which included competition policy.

Unfortunately, to this date, lesser developed countries have been paying heavy costs for the cross-border impact of anti-competitive practices that countries are commonly seen to indulge in. Several studies substantiate this stance. As a result of price fixing conspiracies during the 1990s developing countries paid approx. $ 20-25 billion in excessive prices (Levenstein and Suslow, 2001). Another study conducted by World Bank in 2001 concluded that a breakup of price-fixing arrangements among private carriers could reduce transport prices by 20 per cent on U.S. routes and a fall in the import bill of developing countries by $2.3 billion in maritime transportation (Fink et.al. 2001)

The impact on the commodities market is severe. The major commodity spike of 2007-08 sent alarm bells ringing when the prices of many primary goods doubled from what they had been not so long ago. Much of this fluctuation may be explained by way of simple economics of demand and supply, while managing supply side failures is critical to restore some sense in the market. One such management issue is that of the inability of trading nations to deal with rampant anticompetitive practices, especially when the importing countries pay heavily for anticompetitive practices exempted by exporting countries' competition laws. Case in point here is the global potash fertiliser export cartel.

Canpotex is an exporter of potash and phosphate, and an offshore company for three North American firms: Agrium, Mosaic and Potash Corp of Saskatchewan. Canpotex coordinates with Belarusian Potash Co in the world market of potash formed by member companies: Belaruskali and Uralkali. Canpotex is an export cartel because Saskatchewan's three major potash producers use it to set prices for foreign potash buyers and to control supply. Canpotex

has an explicit exemption pursuant to section 45(5) of the Competition Act (1985) of Canada. It further coordinates with Belarusian Potash Co and PhosChem, a U.S. based export cartel to together control about 70 per cent of the world trade in two key fertilisers: potash and phosphate. Due to their agricultural production needs and reliance on fertiliser imports, countries such as India, China, Brazil and Australia have to buy from these transnational companies despite the high international prices set by them. Since potash and phosphate are essential fertilisers for agricultural production, most countries such as India, Brazil, China and others that are import reliant on potash have no option but to pay the high monopoly rents of the supplier cartel. In India, major proportion of the subsidies are doled out to fertilisers. Unfortunately these fertiliser subsidy bills do not translate into a proportionately high volume of fertiliser use. During 2002-07, 88 per cent of the reported increase in subsidies was due to the sharp rise in international fertiliser prices while only 12 per cent was a result of enhanced consumption of fertilisers.

A recent study by Frederic Jenny has highlighted the overcharge paid by India due to anticompetitive practices in the global potash market. Under a competitive scenario, the price of potash would decline from $574 per tonne in 2011 to $217 by 2015, and subsequently increase to $488 by 2020. However, in the continuing presence of fertiliser cartels, the price of potash would steadily increase from $574 per tonne in 2011 to $734 in 2020. The resulting overcharge for India and China, two of the largest buyers of potash amounts to more than a billion US$ per year per country (Jenny, 2011)

Such export cartels are in some cases government sponsored. For example, in February 2010, China, which controls more than 95 per cent of the global production of rare earths, a collective name for 17 minerals used in high technology from mobile phones to military equipment, announced that it intended to impose restrictions on rare-earth mining in the next five years while maintaining international cooperation on trade in the metals, including "reasonable" export quotas.

But export cartels also exist in the manufacturing sector and can originate in developing countries. For example, last year the Chinese government filed an amicus brief in a US court in support of a motion to dismiss a private suit against four Chinese vitamin manufacturers accused of having cartelised their exports to the US since 2001. The Chinese government argued in its brief that it had supervised the price-fixing as part of its effort to “play a central role in China’s shift from a command economy to a market economy” and in order to mitigate the exposure Chinese companies faced in potential antidumping investigations.

The European Union stated in 2000 that export cartels “had a clear distortionary effect on international trade as well as a harmful impact on development”. In less developed countries where the domestic industries are not very competitive, export cartels are especially more successful as they are able to gain greater market power in these foreign markets. The entrance of a foreign cartel into the importing country whether there is no domestic production or there is an existing domestic oligopoly, would have welfare reducing effects if the foreign cartel restricts its sales in the importing country (Bhattacharjea, 2004; Levenstein and Suslow 2006). Additionally, such cartels hurt world trade among partners. Competition authorities in the countries of origin of the export cartels do not act against them because export cartels do not affect the domestic markets of the cartelists. Competition authorities in the victimised countries either do not have powers to act against the export cartels which they suffer from for a variety of reasons. They may lack extra-territorial jurisdiction (as the litigation in India against the US-based soda ash cartel under the now repealed Monopolies and Restrictive Trade Practices Act, 1969 showed); the sovereign compulsion doctrine may

prevent them from prosecuting state sponsored export cartels; they may not have the means to gather the evidence they would need to convict the perpetrators even if they have jurisdiction or they can be under pressure from their government not to act against them so as not to expose the country to retaliations endangering its own economy and state supported export cartels.

TREATMENT OF CARTELS IN NATIONAL COMPETITION POLICY AND NEED FOR INTERNATIONAL RULES AGAINST EXPORT CARTELS

While empirical research on the effects of export cartels remains inconclusive no country has a strong incentive to ban export cartels unilaterally provided they do not adversely affect competition in domestic economies, either explicitly or implicitly. Implicit exclusions are as good as an explicit one as far as action by the home authorities is concerned. Studies have shown that fifteen countries maintain these exemptions. It may well be inferred from this treatment of export cartels under a competition regime that the same activity would be illegal if it were pursued domestically but since the exported quantities affect foreign markets and generate revenue in the process, they are exempt from the competition regime of the country. Or in other words, while monopoly rents accrue to the home country, the consumer loss due to high prices is mostly felt in the foreign (importing) countries leaving little incentive for exporting countries to regulate such activity.

The approach of governments to collusive cartels for production and exportation in resource rich countries is paramount to note here. In some cases, governments of resource-rich countries are closely involved in collusive export arrangements while in others they may simply allow collusive practices among exporters as long as they do not affect domestic markets. In 1918, the United States Congress passed the Webb-Pomerene Act (WPA) with the mandate of helping domestic firms in facing competition from foreign international cartels. The Act exempted the export activity of associations for trade in goods. In 1982, the Export Trading Companies Act was additionally passed to include export of services. While the rationale for orchestrating such exemptions for export associations were well founded, an OECD study carried out in 1994 revealed that 87 of 97 of these export cartels acted as hard-core cartels i.e. either through price-fixation, co-ordinated bids or allocation of customers. Yet the United States continues to grant explicit exemption to export cartels to this day since they do not harm the domestic market. Another country that follows explicit exemptions to export cartels is Australia. On the other hand, EU grants implicit exemption to export cartels as the provisions under EU competition law (Articles 101 and 102, formerly 81 and 82) regulate activities that ‘distort competition within the common market’ only.

The rationale adopted by the Webb Pomerene is often duplicated by many national export cartels. The rationale for permitting export cartels is that it may facilitate cooperative penetration of foreign markets, transfer income from foreign consumers to domestic producers and result in a favourable balance of trade. Critics however argue that the export cartel exemptions represent nothing but a beggar thy neighbour policy where the home country where the cartel originates gains while the foreign country loses. Studies have revealed lack of evidence indicating that export cartels were necessary as an instrument of countervailing power against cartels of foreign competitors or foreign buyers. Besides, many export cartels such as the Canadian potash cartel, Canpotex, have been seen to comprise of large companies to enter markets where there is no domestic production of potash hence hardly any domestic competition. Another reason why governments exempt export cartels lies in strategic trade theory. Export cartels have the effect of restricting the volume of

exports and raising the export price which ultimately helps in shifting rents from foreign firms to domestic ones and improving their terms of trade. Scholars have also argued that the continuation of exemptions granted to export cartels despite their welfare reducing impacts can also be partly explained through the public choice theory (Sokol, 2008), that is to say, that the people that are affected by such cartels are foreign consumers and do not have the same lobbying power as the firms participating in the export cartels to influence political decision making in their favour.

A few researchers who applied the prisoner's dilemma theory to the export cartels issue highlight the need for international cooperation in formal enforcement actions against cartels. Sweeney (2007) for instance argues that the incentives to discipline export cartels present a prisoner's dilemma in the sense that a country currently prohibiting export cartels can always make itself better off by allowing them and a country that currently permits export cartels can make itself worse off by prohibiting them. He concludes that "in the absence of an agreement, the world's trading nations are in equilibrium when they permit export cartels. Durand, Galarza, and Mehta (2004) endorse his findings. They examined the welfare effects of banning or allowing export cartels. Their study revealed that when a country chooses to allow export cartels while the other country still bans this practice, the welfare level it reaches is higher than when it also chooses to ban them. The authors conclude the study holding that if countries could co-ordinate their antitrust policy to prosecute export cartels they would all reach a higher welfare level".

Clearly, while the potential loss to total welfare and consumer welfare caused by hard-core cartels has been globally recognised, the global fight against the gravest antitrust infringement excludes from its ambit similar impacts that may arise from the operation of exempt cartels such as those formed to control exports. This issue has been discussed at length in the forthcoming sections. It discusses the governance challenges posed by export cartels in primary products that may be especially damaging due to the nature of these commodities leaving importing countries with little options to combat extra-territorially against the ills of such exempt cartels.

POLICY OPTIONS AND CHALLENGES

1. Seeking a unilateral solution and the application of the "effects doctrine":

   Even though in principle, countries may enforce their domestic antitrust laws against an export cartel extraterritorially through the application of "effects doctrine" it is often difficult to do so. Further, this is a hugely complex provision which would require access to information about foreign exporters which is data often unavailable in addition to challenging the exemption or immunity enjoyed by them. Often this is matched with lack of resources financial and legal for many countries to engage in this exercise effectively (Levenstein et al., 2003). Application of "effects doctrine" is especially challenging in case of countries that have no notification requirement for registration of export associations/cartels within their domestic territories and hence no data is available for the importing country to work on. E.g. information on their geographic coverage, products and extent is nil (World Bank, 2003).

2. Seeking solution through multilateral trade rules:

   a. Strict disciplines on export restrictions: Export restrictions that have the effect of restricting the volume of exports and tightening global supply further aggravate

the problem of cartelization. These measures particularly affect low income countries which may be particularly dependent on imports of agricultural and raw materials and hence may lose a great deal from the absence of strict multilateral disciplines on measures such as export taxes, voluntary export restraints, quota allocations and other forms of export controls adopted by countries to better their terms of trade while worsening that of the others.

b. Remedies at the WTO against injury caused by export cartels: The damage caused by export cartels is in a way similar to the incidence of dumping. Scholars have termed this as a case of reverse dumping which may be penalised as such. Although material injury in such instances would be hard to show, facts such as abnormal high import prices, registration of export cartels and other factors may be taken in order to create a rebuttable presumption of reverse dumping leaving the burden of proof with the exporting country to show that it has not been selling like products at prices much higher than the normal value (Bhattacharjea, 2004).

3. Formation of Countervailing Buyer Cartels

Former petroleum minister of India, Mr. Manishankar Aiyer proposed formation of an OPEC-like organisation among Asian oil buying countries and negotiate hard with Saudis and OPEC for better prices, including eliminating the Asian premium of $1.5-2 a barrel. Such a cartel to be formed as a countervailing power as opposed to a monopoly cartel may be a strategy that buying countries may use in order to counter the exploitative forces of powerful trading partners. Another such countervailing cartel may be formed by consumer countries such as India, China, Brazil and others against the Canpotex Potash Cartel (Mehta and Nayak 2011).

4. Reviving the study on interaction between trade and competition.

Given the reforms in competition regimes brought about across the world since the collapse of the agenda in WTO (130 countries have adopted a competition law today as opposed to 35 in 1995) and now that it seems as though the Doha negotiations do not have an immediate future and that the WTO has to redirect its focus from trade negotiations to analyses, the time has come for this multilateral organisation to undertake a serious and dispassionate study of the effects and the appropriate legal regime to regulate export cartels. Such a study would need to distinguish between the export cartels which may actually enhance the export opportunities of small countries which would not otherwise be able to access export markets from the export cartels which have no such redeeming values and are limited to rent seeking and reduce competition rather than enhance it. It would also need to distinguish between the purely private export cartels and the state sponsored cartels, like oil, which may deserve a different treatment. Finally it should take into account the fact that export cartels may originate in countries which have vastly different levels of economic development and therefore have quite different domestic impacts.

5. Multilateral Agreement on Competition

This is not a new proposal. As mentioned earlier, an effort in this regard had been already made in 1996 at the Singapore Ministerial when the Working Group on Interaction between Trade and Competition Policy (WGTCP) was formed. This was one of the very first occasions when the issue of export cartels was discussed at the multilateral level and all the Members were able to exchange their views on the

matter. The main structural difference between rich and poor countries, was that the rich wanted a multilateral agreement on competition, which would have meant some degree of harmonization of domestic competition laws with the international standards. However, developing countries perceived this as a market access push by the rich. Because, if competition laws were designed and operated on the lines of rich country laws, it would have meant providing a level playing field for rich country firms. On the other hand, the poor countries wanted a multilateral agreement for competition, i.e. something which could help them to deal with competition violations of rich country firms.

On the whole, there were divergent country positions. While some called for an outright ban of exemptions granted to export cartels, developing countries were of the view that this would be a one size fits all approach and not support the interest of lesser developed countries for whom export cartels may be a huge source of export earnings. Unfortunately countries were unable to reach a consensus on the matter. The Cancun Ministerial Conference ended in a deadlock, due to this very issue, and the General Council of the WTO dropped competition policy from the Doha agenda in 2004 (Hufbauer and Kim, 2008).

Nonetheless, the WGTCP succeeded in building awareness on competition issues and initiating a new wave of analytical thinking about competition issues and the interface between trade and competition. A good example is the case of India which started preparing a new competition law and also incorporating competition clauses in its bilateral trade agreements. Many other countries also started designing and adopting competition laws after this period.

In today's globalised era where the practices of one country have externalities beyond its own borders, it is necessary to re-visit multilateralisation of competition rules which would effectively address the negative externalities caused by anticompetitive practices of a country beyond its borders. Such a body would also provide a set of rules and intervene when markets fail and the players are caught in a "prisoners' dilemma" which is usually the case in the issue of export cartels. The appropriate forum for this should be a joint initiative between the WTO and UNCTAD in order to have both the developed and the developing countries on board. However all this requires the setting up of a body that would launch a careful examination of the implications of the core principles of the WTO for a multilateral competition agreement and what is expected from such an agreement which would then decide how it is to be drafted in order to align such requirements in its scope and substance. It would also engage with countries to assess the potential of such an international agreement to serve the interests of countries and in terms of providing them with adequate protections from the growing menace of cross-border anti-competitive practices without compromising on their development strategies.

The success of the MCA would depend to a significant extent on whether it would be able to achieve the desired level of international cooperation between the developed and the developing countries so as to be able to serve the primary and most critical objective of addressing the developmental consequences of cross-border anti-competitive activities.

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