Subject: Comity - AMC request for comments
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From: Philip Marsden <p.marsden@BIICL.ORG>
To: <comments@amc.gov>

In response to your request for comments, please find attached two brief papers:

- the first describes one serious failing of the current 'multilateral procedures' (Marsden, "WTO decides first competition case – with disappointing results", Competition Law Insight (May 2004)) and

the second makes suggestions for reform (Marsden, "Competition after Cancun – a personal view", Competition Law Insight (October 2003)).

I hope you find these interesting and would be happy to help you further in your very interesting work.

Best,

Philip

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Competition Law insight

Antitrust law and policy in a global market

WTO decides its first competition case, with disappointing results

By Philip Marsden

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Trade and competition

WTO decides first competition case - with disappointing results

*By Philip Marsden**

The prospect of dispute settlement on competition cases at the World Trade Organisation has long been thought far-fetched – even more so after the Cancún Ministerial last September when the EU dropped its demand for WTO competition rules *(see CLI October 2004, p.22)*.

Last month, a WTO dispute settlement panel found that Mexico had not done enough to prevent anticompetitive practices in its market from impeding the entry of foreign competitors.

The *Telmex* case is based on WTO competition rules agreed in 1997 to help open telecommunications markets. The rules in the WTO Reference Paper on Procompetitive Regulatory Principles are quite basic, obliging signatories merely to enact "appropriate measures" to prevent "major suppliers" from engaging in "anticompetitive practices."

However, the WTO panel was not afraid to fill in the gaps. It made detailed findings on market definition, explained what constitutes a "major supplier," expanded the definition of "anticompetitive practices" and – overruling the state action doctrine – held that governments could not require businesses to engage in anticompetitive conduct.

Competition lawyers in any jurisdiction should be surprised at the decision, and dismayed by the reasoning behind it. Trade lawyers should be concerned about what the panel's decision bodes for the balance between the WTO's judiciary and its "parliament" – the General Council.

It seems that when trade negotiators fail to reach agreement, dispute settlement panels will create new commitments to open markets. This is troubling in itself but even more so when panel decisions affect the terms of competition in the market without applying disciplined competition analysis.

The Telmex dispute – commercial background

In the mid-1990s, American telecoms provider Sprint partnered with Mexico's largest supplier of telecoms services, Telmex, to provide long-distance services between the two countries. AT&T and MCI had to settle for deals with lesser Mexican players and could not benefit from Telmex's considerably larger network. They called on the US Trade Representative to help them get the kind of access that Sprint had.

The resulting American WTO complaint demanded that Mexico require Telmex to provide these US firms with non-discriminatory access as provided for by the "procompetitive regulatory principles" in the WTO Reference Paper.

After only a few months of the pressure of strained trade relations with the US, the Mexican telecoms regulator, Cofetel, issued a set of "asymmetric regulations for Telmex" which ordered it to provide all foreign long-distance operators with access to its network at cost.

Not satisfied with that, AT&T complained that it was still being overcharged for access, costing US callers a billion extra dollars a year. The US complained to the WTO's Dispute Settlement Body, arguing that the access rate was not cost-oriented and that effectively Mexico had set up a cartel of telecoms operators – with Telmex as the ring-leader – who were agreeing prices, overcharging US rivals and thus inhibiting foreign entry.

The US won on both grounds at the WTO. The panel recommended that Mexico's access rates conform to its international obligations. (This recommendation may have been superseded by events, as the rates have fallen by 75% since the dispute was launched.) What is really interesting is how the panel came to find that Mexico had been running a cartel.

What were the main allegations?

Mexico's international long distance ("ILD") rules require that Telmex negotiate a settlement rate for incoming calls with foreign suppliers and apply that rate to interconnection for incoming traffic from the US. Telmex must also give up traffic to, or accept traffic from, other suppliers depending on whether the proportion of incoming traffic surpasses, or falls short of, its proportion of outgoing traffic. To this end, Telmex may enter "financial compensation agreements" with other operators, which are then approved by the Mexican authorities.

The US alleged that this was a state-authorised cartel benefiting Sprint and Telmex and harming their American rivals. Mexico argued that its ILD rules set up a pricing mechanism that allocated revenues with responsibilities, and prevented predatory pricing by foreign entrants with deep pockets. It submitted that the US was seeking to overturn a typical interconnection agreement just to benefit AT&T.

While cartels are almost universally acknowledged to be bad things, governments have not been able to agree on binding WTO commitments to prohibit them. The panel did not deny the US its complaint. Instead, it found a way of creating a WTO cartel ban using the principles in the Reference Paper on telecoms.

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The Reference Paper – introducing "procompetitive regulation"

At the end of the GATT negotiations liberalising trade in goods and services, many governments recognised that traditional trade law disciplines were not enough to ensure that their markets became and remained competitive. As the US has explained:

> ... the negotiating parties accepted that a grant of *de jure* market access and national treatment was insufficient to grant *de facto* or effective market access, absent commitments by governments to regulate former monopolies in a pro-competitive manner, because such former monopolies have both the ability and the incentive to dictate anticompetitive terms of market entry for new competitors.

In the telecoms sector in particular, a right of general entry had to be given to new competitors – whether domestic or foreign – through procompetitive "asymmetric regulation" of major domestic suppliers. Trade negotiators thus provided in the Reference Paper that WTO members should be required to ensure that their large incumbents provide sufficient entry points on satisfactory terms so that their competitors could connect to their networks.

The approach in the Reference Paper is part competition policy, part regulation. It protects competition by requiring that:

> Appropriate measures shall be maintained for the purpose of preventing suppliers who, alone or together, are a major supplier from engaging in or continuing anticompetitive practices.

It promotes competition by requiring that major suppliers provide their competitors with market access, for example, by allowing other firms to connect to their telecoms networks on non-discriminatory terms and conditions, in a timely manner and upon request. Fifty-seven WTO members committed themselves to the Reference Paper – including the US, Mexico and the EU – while six others promised to adopt regulations based on it.

The Reference Paper is more detailed than any other binding multilateral "competition" rule. As such, trade negotiators are keen to apply its principles to other formerly public sectors with monopolistic or oligopolistic characteristics.

Due to the important role it is playing in opening national telecoms markets, and its use as a template for opening other sectors, the Reference Paper is the most important competition-related trade commitment in the WTO framework. As its main provisions were left undefined by negotiators, WTO dispute settlement would play a crucial role in clarifying and interpreting these commitments.

The *Telmex* panel certainly had its work cut out for it, not least in offering guidance on the meaning of terms such as "major supplier," "anticompetitive practices" and the crucial question of whether government-mandated conduct could fall foul of the prohibitions.

The dispute settlement panelists appointed to rule on these issues were Raymond Tam, a Manulife insurance executive from Hong Kong, Bjorn Wellenius, a telecoms expert from the World Bank, and the chairman, Professor Ernst-Ulrich Petersmann, who is a noted academic and writer on trade and competition issues.

THE PANEL'S FINDINGS

Is Telmex a "major supplier"?

The Reference Paper states that:

> A major supplier is a supplier which has the ability to materially affect the terms of participation (having regard to price and supply) in the relevant market for basic telecommunications services as a result of:
> *(a)* control over essential facilities; or
> *(b)* use of its position in the market.

The panel accepted that it had to define the "relevant market," examine whether Telmex had "the ability to materially affect the terms of participation ... in that market," and decide whether that ability resulted either from "control over essential facilities" or from "use of its position in the market."

What is the "relevant market"?

The US argued that, applying "basic principles of United States antitrust law and Mexican competition law, which define the relevant market in terms of demand substitution, the relevant market was the termination of voice telephony, facsimile and circuit-switched data transmission services supplied cross-border from the United States to Mexico."

Mexico disagreed, arguing that US calls terminating in Mexico could not be a separate market as "Telmex completes international calls on a shared-revenue basis, under a traditional accounting rate regime, and the relevant market would thus have to include two-way traffic."

The panel had little trouble accepting the market definition submitted by the US:

> The services at issue are basic telecommunications services ... originating in the United States, and for which US suppliers are seeking interconnection with Mexican concessionaires for termination of the service in Mexico. US suppliers have a choice of Mexican operators with whom they may interconnect and terminate, even though these operators, by Mexican law, must charge a single price set by the operator with the largest volume of outgoing traffic, and Telmex controls the majority of international gateways necessary to terminate the services. Contrary to Mexico's arguments, therefore, there does exist supply and demand – a "market" – in Mexico for termination.

The panel expressly approved the American notion of demand substitution – "simply put, whether a consumer would consider two products as substitutable" – and found it to be "central to the process of market definition as it is used by competition authorities ... Applying that principle, we find no evidence that a domestic telecommunications service is substitutable for an international one, and that an outgoing call is considered substitutable for an incoming one. One is not a practical alternative to the other."

Accordingly, the WTO panel found the "relevant market" to be the termination in Mexico of calls from the US.

Does Telmex have market power?

The US argued that the Mexican ILD rules require that Telmex fix the rates for termination among the other Mexican suppliers, and thus can "materially affect" their terms of participation. The US also argued that this concept "corresponds to the concepts of 'market power,' used by US competition authorities, and 'substantial power,' used by Mexican competition authorities. A firm has market power if it has the ability profitably to maintain prices above competitive levels for a significant period of time, which implies both the ability to maintain prices well above costs, and protection ... against a rival's entry or expansion."

The US cited a 2001 finding by Mexico's competition authority – the Comisión Federal de Competencia – that Telmex had substantial power in international services markets based on "a market share of 74% in international traffic, control of nearly 75% of international gateway capacity, a right to set prices because of its large market share, as well as advantages arising from vertical integration."

The US also noted that "a large market share on the order of 50% or more, particularly when sustained over time, is well recognised by competition authorities and telecommunications regulators as relevant evidence of a firm's market power, though not the sole determining factor, and the higher the market share, the more readily it will support a presumption of market power."

The US also argued that the absence of significant new suppliers of international telecoms services in Mexico during the past few years was another indicator of Telmex's market power.

Mexico said that the Comisión Federal de Competencia decision was "currently under review by Mexican courts precisely because it was based on data from 1996, that is, when the telecommunications market was not yet fully open."

It noted that 27 concessionaires may now provide long-distance services in Mexico, including three US-affiliated carriers – Avantel (WorldCom), Alestra (AT&T) and Iusatel (Verizon) – and that new entrants have gained significant market share when compared with other countries that opened the sector to competition under similar conditions. Mexico noted that in the US, after 11 years of competition, the incumbent AT&T still had a market share of 59% – similar to that of Telmex today.

The panel based its decision purely on the empowering regulation:

> [S]ince Telmex is legally required to negotiate settlement rates for the entire market for termination of the services at issue from the US, we find that it has patently met the definitional requirement in Mexico's Reference Paper that it have "the ability to materially affect the terms of participation," particularly "having regard to price."

Does Telmex's market power result from "control of essential facilities" or "use of its position"?

On this third question, the parties had not given the panel much to get its teeth into, simply summarising their arguments about Telmex's market power. As a result, the panel did not bother to analyse these specific requirements of the Reference Paper either. Instead, it merely stated that "the ability to impose uniform settlement rates on its competitors is the 'use' by Telmex of its special 'position in the market,' which is granted to it under the ILD Rules."

As such, the panel found that Mexico had a special obligation to control such a "major supplier" to ensure that it did not engage in "anticompetitive practices."

In an interesting aside, the panel did not limit this obligation to Telmex. The Reference Paper mentions "suppliers who, alone or together, are a major supplier."

The panel decided that "[s]ince we have already found that Telmex alone is a 'major supplier' ... and that the practices at issue involve acts of all the Mexican suppliers who are gateway operators, we can conclude also that Telmex and all the other Mexican gateway operators are together a 'major supplier'."

Given the large number of Mexican operators – most with relatively small market shares – this seems to be a step of inductive reasoning too far and one that is not supported by the facts, regulation or not.

Further concern will be raised by the next stages of the panel's enquiry:

- how it chose to define the "anticompetitive practices" that all Mexican operators were alleged to be engaged in
- whether practices could be "anticompetitive" if they were required by domestic regulation, and
- if so, whether WTO commitments should trump such regulation

What are "anticompetitive practices"?

The Reference Paper offers a non-exhaustive list of examples of "anticompetitive practices": "engaging in anticompetitive cross-subsidisation; using information obtained from competitors with anticompetitive results; and not making available to other services suppliers on a timely basis technical information about essential facilities and commercially relevant information which are necessary for them to provide services."

The panel began by noting that "[t]he term 'anticompetitive practices' is not defined in ... Mexico's Reference Paper," the practices referred to being just examples. Instead, the panel turned to guides that other WTO panels have found to be indispensable – the *Merriam-Webster* and *Shorter Oxford Dictionaries* – to make the following pronouncements:

> The dictionary meaning of the word "practices" is very general. Its meanings include "the habitual doing or carrying on of something; usual, customary, or constant action; action as distinguished from profession, theory, knowledge, etc; conduct." The word "practices" thus indicates "actions" in general, or can mean actions that are "usual" or "customary." The dictionary meaning of the word "competitive" includes "characterised by competition; organised on the basis of competition." The word "competition," in its relevant economic sense, is in turn defined as "rivalry in the market, striving for custom between those who have the same commodities to dispose of."
>
> Consistent with these meanings, the word "anticompetitive" has been defined as "tending to reduce or discourage competition." On its own, therefore, the term "anticompetitive practices" is broad in scope, suggesting actions that lessen rivalry or competition in the market.

Having cleared that up, the panel then looked at the examples of "anticompetitive practices" in the Reference Paper and made the unedifying point that they "illustrate certain practices that were considered to be particularly relevant in the telecommunications sector."

They then noted that cross-subsidisation, misuse of competitor information, and withholding relevant information are all things that a major supplier can, and might normally, undertake on its own, but that "such a supplier could be comprised of different companies."

The panel said that this itself "suggests that horizontal co-ordination of suppliers may be relevant." The panel then engaged in some more inductive reasoning: "cross-subsidisation ... indicates that 'anticompetitive practices' can include pricing actions by a major supplier."

The panel had thus sown the seeds for finding that a Reference Paper designed primarily to address denial of access and other anticompetitive practices by a dominant operator could also be interpreted to be focused on horizontal price-fixing.

It pursued this course of reasoning by putting the Reference Paper to one side, and examining how "[t]he meaning of 'anticompetitive practices' is also informed by the use of this term in members' own competition legislation." Rather than look at any competition laws, though, the panel relied on a background note supplied by the WTO Secretariat:

> Many WTO members maintain laws to ensure that firms do not undermine competition in their markets. The term "anticompetitive practices" is often used in these laws to designate categories of behaviour that are unlawful. The range of anticompetitive practices that are prohibited varies between members, but practices that are unlawful under the competition laws of members having such laws include cartels or collusive horizontal agreements between firms, such as agreements to fix prices or share markets, in addition to other practices such as abuse of a dominant position and vertical market restraints.

The panel also found that

> the meaning of "anticompetitive practices" is informed by related provisions of some international instruments that address competition policy. Article 46 of the 1948 Havana Charter for an International Trade Organisation already recognised that restrictive business practices, such as price-fixing and allocation of markets and of customers, could adversely affect international trade by restraining competition and limiting market access.
>
> The importance of ensuring that firms refrain from engaging in horizontal price-fixing agreements, market or customer allocation arrangements and other forms of collusion is likewise emphasised in the United Nations Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices.

The panel felt that

> [i]t is also worth pointing out, since both Mexico and the United States are members of the OECD, that the OECD has adopted a Recommendation calling for strict prohibition of cartels. In the work of the WTO Working Group ... reference has been made to the pernicious effects of cartels, and to the consensus that exists among competition officials that price-fixing "hard-core cartels" ought to be banned. Cartels were also described as the most unambiguously harmful kind of competition law violation.

Finally, the panel sought out the intent of the Reference Paper itself – albeit without examining anything as pedestrian as *travaux preparatoires:*

> An analysis of the Reference Paper commitments shows that members recognised that the telecommunications sector, in many cases, was characterised by monopolies or market dominance. ... Accordingly many members agreed to additional commitments to implement a procompetitive regulatory framework designed to prevent continued monopoly behaviour, particularly by former monopoly operators, and abuse of dominance by these or any other major suppliers. ... Mexico's Reference Paper commitment to the prevention of "anticompetitive practices" by major suppliers has to be read in this light.

With the focus thus clearly on monopolistic conduct by a dominant incumbent, the panel nevertheless found that

> the object and purpose of the Reference Paper commitments made by members supports our conclusion that the term "anticompetitive practices," in addition to the examples mentioned ... includes horizontal price-fixing and market-sharing agreements by suppliers which, on a national or international level, are generally discouraged or disallowed.

Can actions required by a member's law be "anticompetitive practices"?

Mexico had argued that practices required by regulation could not be "anticompetitive" as they were mandated by "ILD rules that are part of the regulatory framework of laws intended to increase competition" by preventing predatory pricing by foreign entrants.

As intervenor, the European Communities noted that, even if Telmex's acts were "anticompetitive," they could not be "practices" in the true sense of the word, as they were not freely undertaken. Indeed, argued the EU:

> [If] Mexico chooses not to allow competition between telecommunications operators on a certain matter, there is no scope for anticompetitive practices relating to that matter. It is not possible to restrict competition where competition is not allowed.

The US argued that anticompetitive practices do not change their nature simply because they are required by national laws and regulations: "just because Mexican regulation requires the suppliers to collude does not mean they are not indeed colluding or, in other words, engaging in horizontal price fixing."

Any other interpretation, the US argued, would render the provision "self-defeating and meaningless," since a member "could easily avoid the obligation to maintain appropriate measures to prevent 'anticompetitive practices' by formally requiring such practices."

The US argued that "requiring telecommunications carriers to adhere to a Telmex-led horizontal price-fixing cartel ... [that] stifled market challengers" and "preventing price competition by new entrants to protect a major supplier's high price cannot possibly be understood as promoting competition." The US submitted that the Mexican system is "not directed at preventing harm to competition but rather is directed at preventing the natural results of competition."

The panel chose to rise above this debate. It stated that it was

> aware that, pursuant to doctrines applicable under the competition laws of some members, a firm complying with a specific legislative requirement of such a member (e.g. a trade law authorising private market-sharing agreements) may be

> immunised from being found in violation of the general domestic competition law.

With a flourish, however, it applied principles of public international law to sweep the state action doctrine aside:

> International commitments made under the GATS "for the purpose of preventing suppliers ... from engaging in or continuing anticompetitive practices" are, however, designed to limit the regulatory powers of WTO members. Reference Paper commitments undertaken by a member are international obligations owed to all other members of the WTO in all areas of the relevant GATS commitments. In accordance with the principle established in article 27 of the Vienna Convention, a requirement imposed by a member under its internal law on a major supplier cannot unilaterally erode its international commitments made in its schedule to other WTO members to prevent major suppliers from "continuing anticompetitive practices."

The panel therefore concluded that acts required by governments can be "anticompetitive practices" and be prohibited by WTO rules.

Are Telmex's practices "anticompetitive"?

On this crucial point, the WTO panel was brief. It found "the United States argument convincing that the removal of price competition by the Mexican authorities, combined with the setting of the uniform price by the major supplier, has effects tantamount to those of a price-fixing cartel."

The panel also found "that the allocation of market share between Mexican suppliers imposed by the Mexican authorities, combined with the authorisation of Mexican operators to negotiate financial compensation between them instead of physically transferring surplus traffic, has effects tantamount to those of a market sharing arrangement between suppliers." The panel noted that it had read horizontal practices such as price-fixing into the definition of "anticompetitive practices."

It found, therefore, that the ILD rules required practices by Telmex that are "anticompetitive" within the meaning of the Reference Paper.

Did Mexico fail to maintain "appropriate measures" to prevent "anticompetitive practices" in its market?

This final test for prohibition had largely been considered already. The US had argued that "far from proscribing such behaviour, Mexico maintains measures that require Mexican telecommunications operators to adhere to a horizontal price-fixing cartel led by Telmex."

Mexico tried to argue again that the measures were pro-competitive and prevented predation by foreign entrants. It also tried to argue more generally that by having a competition law in place it did maintain "appropriate measures" to prevent anticompetitive practices.

The panel had no time for Mexico's pleas. It noted that "[t]he word 'appropriate,' in its general dictionary sense, means 'specially suitable, proper.' This suggests that 'appropriate measures' are those that are suitable for achieving their purpose – in this case that of 'preventing a major supplier from engaging in or continuing anticompetitive practices'."

It accepted that "measures that are 'appropriate' ... would not need to forestall in every case the occurrence of anti-competitive practices of major suppliers. However, at a minimum, if a measure legally requires certain behaviour, then it cannot logically be 'appropriate' in preventing that same behaviour."

Thus the panel held that Mexico had violated its obligations under the Reference Paper by failing to maintain (and indeed requiring) "anticompetitive practices" by a "major supplier." Subject to appeal, Mexico must bring its measures into conformity with WTO law by significantly revising or eliminating its current system.

Commentary

The decision really speaks for itself. Many weaknesses of reasoning and inadequate competition analysis have already been identified. Unfortunately, these are unlikely to be corrected on appeal. The WTO Appellate Body has fewer experts who appreciate competition issues than the panels themselves.

The WTO's "legislative" arm could offer more guidance on the object and intended application of the competition provisions in the Reference Paper but that is not likely to happen any time soon, and would not help correct the dangerous precedent that the *Telmex* decision sets.

WTO purists may point out that panels are not obliged to apply competition analysis when interpreting provisions of a trade agreement and, moreover, that there is no rule of *stare decisis* at the WTO anyway. They may say that this decision only applies to these arrangements in Mexico, and has no broader impact. But that would be naïve.

The *Telmex* decision points to several fundamental flaws in the WTO system. With such a large membership, many provisions are "constructively vague." Panels are asked to interpret and clarify provisions about which they have little expertise. While they can call on experts to help them, most are reticent to do so.

Panels are bound by the Dispute Settlement Understanding which prohibits them from "adding to or diminishing the rights and obligations" in the agreements, so that they do not upset the "security and predictability" of the multilateral trading system.

Panels thus take what they think is the safest route, turning to dictionaries to define key words. These are often terms of art, about which there is actually much debate. "Competition," for example, certainly means a process of rivalry, but any international body trying to define it should take some account of the widely differing positions around the world on what degree of rivalry is appropriate, and what ends it should seek.

Some authorities and courts prefer an ordo-liberal approach that permits government intervention to ensure that no one rival gets too big. Others are more trusting of the market, and intervene only when consumer welfare is actually threatened. In making that calculus, some consider efficiencies, others do not. None of this was examined by the panel in *Telmex*.

Some may say that in trying to discover whether a WTO commitment has been broken, panels need only look at the text of the treaty and the measures or practices at issue. The text will rarely be unambiguous, though, so panels will usually have to look elsewhere for guidance.

This panel was quick to cite the Vienna Convention on the Law of Treaties to justify some of its interpretative techniques, but ignored the Convention's stipulation that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

Dictionaries may help to provide "ordinary meaning," but the preparatory work of the actual negotiators would have been more relevant and more useful in interpreting a complicated trade agreement.

The Vienna Convention also states that a treaty's "context" can include any agreements between the parties "made ... in connexion with the conclusion of the treaty" or subsequently "regarding the interpretation of the treaty" or practice "in application of its provisions." None of that permits the panel's use of the UNCTAD Set or the OECD Hard-Core Cartel Recommendation, let alone the Havana Charter, which was never even ratified. None of those documents was made "in connexion with" or regarding the interpretation or application of the Reference Paper, or indeed any WTO agreement.

The background papers that the WTO Secretariat provided to the panel do not represent the intentions of the parties or of WTO members more generally. The Secretariat has primarily an administrative support function, although it also maintains a less well-advertised policy role and is staffed with officials who – understandably – have an interest in an ever-expanding role for the WTO, and ever-liberalising world trade. They are hardly representative or objective.

Cartel ban

This brings us to matters of substance with respect to the decision itself. The panel read a cartel ban into a WTO commitment to ban "anticompetitive practices." How bad is that? Some may say "not very" – after all, cartels are anticompetitive and a ban on them is the cornerstone of any good competition law.

But that is not the point. The point is that no signatory of the Reference Paper has agreed to a cartel ban being a WTO commitment, backed up by dispute settlement and trade sanctions. Indeed, the United States has been the most vocal opponent of even the most obvious competition law prohibitions becoming binding trade commitments.

Cartels are not even listed in the anticompetitive practices mentioned in the Reference Paper. Was that omission really a bit of "constructive vagueness" that was just waiting for a dispute settlement panel to clarify? Hardly. The fact that the signatories of the Reference Paper could not agree on such an obvious commitment as a cartel ban must point to something more fundamental. It may be that they agreed that cartels are bad, but trusted their competition authorities to ban them and felt it unnecessary to put such an obvious wish down on paper. However, that is not really how trade negotiations work. If there is any agreement at all, it is usually firmly written down and trumpeted as a "deliverable."

Even if you could read a cartel ban into the Reference Paper, one would have thought that, if the parties wanted to ban state-sponsored cartels as well, they would have mentioned that in the text. Instead they chose quite technical terms such as "cross-subsidisation" and "essential facilities." These are not practices that one associates with cartels, though. They are better known as ways by which a dominant incumbent denies access to its rivals.

Denial of market access

That is really what the Reference Paper is all about. Of course, a "major supplier" can involve more than one operator – but one cannot always reach for a cartel ban to address problems of collective dominance.

Whether or not the Telmex arrangements with other operators allowed them to function as a cartel, they could have been addressed by reading the Reference Paper as banning denial of access or discrimination that amount to an abuse of dominance. That would accord more with the purpose of the Reference Paper, and the type of conduct that might be more prevalent in this sector.

Did the panel typify Telmex's arrangements as a cartel so that it would not have to prove an effect on competition? A *per se* approach to cartel enforcement is not used in every country, but it is the norm. The panel should not have needed to do that, though, since WTO commitments – even ones relating to competition – do not require evidence of net anticompetitive effect.

WTO rules ban state measures that violate commitments. That makes sense for laws and regulations, but things are more complicated when business practices are at issue. Surely more rigorous analysis is required. This is particularly the case when allegations of anticompetitive practices are made by competitors.

Of course, AT&T pursued a WTO action because it was challenging Mexican regulation. It would have had a hard time had it tried to attack Telmex's conduct before the Mexican competition authority or courts. Its allegations would have had to survive a rigorous market analysis and prove that competition had been "diminished, impaired or prevented."

AT&T rightly calculated that it stood a much better chance of success if Geneva-based trade panelists reviewed its complaint under rules that were designed to ensure that Mexico opened its market to foreign competitors.

Being a WTO agreement, the Reference Paper clearly has more to do with promoting "market access" than with protecting the competitive process. It is closer to entrant-friendly *ex ante* regulation than to competition law, which disciplines anticompetitive behaviour after it has been proven likely to harm competition itself.

A bias towards entry is to be expected in any trade agreement, and should not necessarily be condemned, particularly when it applies to sectors that are controlled by former public monopolies and may be crying out for entry.

Nevertheless, without some analytical rigour, such rules can be abused by rivals to get access to things that they could not be bothered to build or buy for themselves. This is clearly how Mexico viewed the US complaint on behalf of AT&T:

> Mexican policy, as shown by the ILD rules, is that domestic carriers should share in and split agreements for incoming calls in terms of their success in securing a share on the domestic market and generating outbound calls. The US sees

it differently ... the only market worth protecting is the one for terminating US traffic to Mexico. The US is acting as if new operators should compete to carry incoming international traffic calls instead of competing for new customers in Mexico. According to the criterion set by the US, an operator who has made a minimal investment in Mexican infrastructure should be allowed to do so on an unlimited basis, taking all the revenue for international calls from the operators who have made such investments and have obtained successful results in acquiring a share of the market.

Conclusion

Whether Mexico was right or not, it deserved better than it got from the WTO. It had made a series of commitments on which it accepted that it would be tested. The panel, however, read in new commitments that Mexico had not offered: a ban on cartels generally and a ban on state-authorised cartels in particular. No matter how worthy such bans may be, they are simply not commitments that Mexico – or any country for that matter – has offered at the WTO.

Should other countries and other companies be worried? How broad is the reach of this decision?

The panel noted that the decision bound only Mexico. That said, 57 countries have signed that Reference Paper, and others are considering adopting it. The Reference Paper is also being used as a template for other sectors including air transport, energy, postal and courier, and even "distribution" services.

This panel read a cartel ban into the Reference Paper's list of commitments. Could other WTO panels add controls on vertical restraints or mergers as well?

The *Telmex* panel thought not, arguing that "beyond our findings regarding horizontal price-fixing and market allocations among competing suppliers of basic telecommunications services – the term 'anticompetitive practices' ... may be interpreted differently by different WTO members."

That they certainly can be. This is one of the reasons why WTO rule-making on competition policy has ground to a halt. However, the wheels of dispute settlement keep on turning, and who knows what the next panel will think up?

Instead of trying to negotiate more competition rules for dispute settlement panels to misinterpret, WTO members should provide guidance that panels can use. It is time for them to agree on "A Competition Policy for the WTO."

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Remedies in European telecoms regulation

The ERG is the European Regulators' Group of national telecoms bodies under the (relatively) new EU regime for electronic communications. In April, it published its common position on remedies with a view to applying a consistent approach. This is the third stage, the others having done the same for market definition and market analysis.

Consumers have to be protected from exploitative behaviour and inefficiency on the part of companies that hold significant market power (SMP). *Ex ante* regulation is intended to give way to normal competition policy instruments, but this may be impossible as long as the assets that give the company the power cannot be replicated economically.

Four situations are identified as giving rise to 27 potential problems. Leveraging by companies at wholesale level may be vertical or horizontal (downstream or neighbouring market). Single market dominance is another, and two-way access, where price setting is linked to retail markets that could otherwise be competitive, is the last.

The standard remedies discussed in this paper are transparency, non-discrimination, accounting separation, access, price control and cost accounting. The principles on which these are to be applied are:

- reasoning in the decision applying the remedy
- assurance of sufficient access to wholesale inputs
- movement towards normal competitive conditions as far as replication of the SMP company's assets is feasible
- formulation in such a way that the advantages of compliance outweigh the benefits of evasion

The remainder of the paper applies these remedies and principles to the 27 competition problems envisaged by the ERG.

A footnote on "margin squeeze" recommends a course that is designed to avoid prescription by dominant supplier and regulator alike. Since a dominant provider's price to retail customers may reflect economies of scale or scope, the imposition of any wholesale supply obligation should be made on the assumption that it will have a 20-25% share of the downstream market.

ERG common position on the approach to appropriate remedies in the new regulatory framework *(ERG (03) 30 rev 1)*
erg.eu.int/doc/whatsnew/erg_0330rev1_remedies_common_position.pdf

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Trade and competition

Competition after Cancún – a personal view

*By **Philip Marsden***

A couple of years ago I argued that the International Competition Network would lead to more practical advances in international cooperation on antitrust enforcement than anything likely to happen at the World Trade Organisation, at least in my lifetime.

Not surprisingly, officials involved in the WTO talks took me to task about this. They viewed the ICN as a talking shop of competition officials who would produce – at most – non-binding recommendations for "best practices" on enforcement issues. The work planned for the WTO was to be far more involved and far-reaching.

Having more than 145 countries meet in Geneva to discuss competition policy at an organisation governed by justiciable trade rules made delegates think long and hard about the kinds of commitments they might make. This would help to ensure that, as competition laws were adopted throughout the world, they would be based on a common "competition culture" and be backed up by truly binding rules. One day, WTO members could be taken to international dispute settlement for not banning cartels or for discriminating against foreign companies.

I still think that the talks at the ICN offer more practical and more immediate benefits than the work at the WTO. After only a year of substantive talks, the ICN did produce best practice guidelines on merger review. These may not be binding, but the process of formulating them and their level of detail makes it unlikely that competition authorities will diverge from this agreed-upon approach. Even if they do, they will feel compelled to explain why, and that will improve international understanding and cooperation more than any legal requirement to toe a common but vaguely-defined line ever could.

Since I take this view, people have asked me why I wrote a book called "A Competition Policy for the WTO" earlier this year. The answer is easy. I think that the WTO could benefit a very great deal from having the discipline of competition policy applied to it. I do not just mean in terms of competition laws entering its rulebook, though. (The sound rationale for that is repeated like a mantra at every trade-related forum considering competition issues: as markets are opened, private anticompetitive practices must not be allowed to replace public trade barriers.) Nor do I mean, as some have argued recently, that "competition policy is crucial to the balance of the [Doha Development] round."

Competition on the trading table

Of course, I know that in trade circles WTO commitments on competition policy are viewed as simply one of many things that the EU has been asking for in return for reform of its Common Agricultural Policy. Obviously, no one ever says that out loud at WTO meetings on the subject.

Commitments to have a competition law and to ban cartels are sold as being valuable in their own right, as well as being an important bolstering of trade liberalisation commitments more generally. The same could be said of the reform of the CAP, of course – any movement there would introduce competition into a large and important sector in Europe, and place developing country farmers on a more level playing field.

However, whether something makes sense on its own, or not, does not matter when vested and long-protected interests are at issue. For example, for years now WTO members have been trying to add greater checks on each others' ability to protect their sunset industries through the imposition of antidumping measures. Such a disarmament programme does not work of its own volition, however. It is not enough for everyone to agree that it is a bad idea to raise the price of foreign imports at the border without proof that they are harming competition in the domestic market, or that misuse of antidumping measures harms world trade, competition and consumers, and ensures that protected domestic industries never have to bother raising their game. Something outside the "antidumping" box has to give before there can be reform within it.

All multilateral trade agreements are based on trade-offs, and competition policy is just one of many bargaining chips on a very large, and increasingly messy table.

Competition off the trading table in Cancún

At the latest meeting of the WTO in Cancún, however, the EU indicated that it was prepared to drop its request on competition policy for the greater good of reaching a more limited, but still liberalising, trade agreement.

However pragmatic that decision was at the time, it was unfortunate for two reasons. First, and most obviously, it did not work: "too little, too late" is one way of explaining why developing countries failed to rise to the bait, though there are myriad others. (Was the EU's offer on CAP reform not enough? Did developing countries engage in too much brinkmanship? Or was it simply a more boring bureaucratic lesson – one that should have been learned in Seattle – that there were too many areas left open for 150 trade ministers to agree on over five short hot days at the seaside?) A post-mortem of this failed ministerial would show several contributing causes of death, all of which offer important lessons for the preparation for – and conduct at – future meetings.

The second reason why the EU's withdrawal of its request on competition is unfortunate also focuses on what it means

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for the future. It is not easy to go back on a concession at the WTO, and the EU dropping the issue effectively takes it off the table for this round. Yes, there are other *demandeurs*, such as Canada, Japan and Korea, and yes, within the WTO Working Group on the Interaction between Trade and Competition Policy, agreement seemed to be very close. After all, the only proposals on the table were positive ones: to start negotiations on a limited and quite banal set of rules, or to have more "clarificatory" discussions to build the necessary "explicit consensus" to launch negotiations at a later stage.

Developing countries were happy to keep meeting in Geneva to discuss the issue, but just did not feel ready to make the political and financial commitment needed to introduce competition enforcement to their markets.

No one was seriously arguing that competition be dropped off the WTO's agenda altogether. But the EU's move effectively does that. The Chairman of the WTO Working Group, Frédéric Jenny, may still call a meeting, but it is not obvious that anyone will come, or that anything of substance may be discussed.

Direction from the membership as a whole is needed, and the sort of discussion that this will require is not likely even to mention competition policy. Its function as a bargaining chip seems to be exhausted, at least for this round.

The dawn of a new era for competition at the WTO

This is a positive development, however, and one that bodes well for the future of competition policy at the WTO. I mentioned above that the WTO could benefit a great deal from having the discipline of competition policy applied to it. I also explained what I did not mean by that. I said that competition policy was more than just an important guarantor of trade liberalisation commitments. I also noted that it should be seen as something more than a mere bargaining chip to be put up against remaining bastions of protectionism.

As I have repeatedly argued for years now, the bargaining chip itself was devalued – and therefore would never amount to much – the minute that the trade negotiators got their hands on it. Following the diplomatic code of "making the possible necessary," the EU requested banal commitments to have a competition law that banned cartels and did not discriminate on its face, to cooperate voluntarily in enforcement and to explain one's policies and decisions.

As there was only an indirect and distant link to trade in this proposal, most developing country governments could only see budgetary demands that they would rather see applied to more pressing issues like clean water, medicine and infrastructure. The need for developing countries to see a clear trade-related benefit from such a commitment was all the more important since the US and EU were not offering to open their markets to agricultural or textile exports, let alone stop subsidising their companies when those were competing directly with companies from the South.

With this impasse, now is the very time that the *demandeurs* on trade and competition should re-group and re-think matters both of substance and of strategy. Fortunately, the two aspects come together when one considers the subject of exclusionary business practices.

Of all possible business arrangements, those that exclude foreign entrants (or indeed any entrants at all) are the ones that have caused the most trade friction over the years. These may be exclusive dealing arrangements, refusals to deal or to license IP rights, vertical mergers, or any practice or arrangement that can operate to impede entry and expansion in the market.

These practices cut across all aspects of competition law, and will be the most difficult to negotiate agreement on. Nevertheless, some of the spadework has already been done in studies at the OECD. Furthermore, exclusionary business practices all share a clear link as potential trade restrictions, and thus cry out most clearly for the combined attention of trade and competition experts alike.

By focusing on "making the necessary possible," WTO members can produce a proposal for competition rules that has value in and of itself, as an issue that is directly "trade-related," and as a bargaining chip in the multilateral trading game. It will not be easy, and will definitely not please negotiators who just want the boffins to give them a checklist of "deliverables" that can be readily handed over at any one meeting. But, since negotiations on competition are off the agenda for this next trade round – due to end in 2005 or so – the substantive experts now have an opportunity to get things right from the start.

Focusing on exclusionary business practices is the way forward. It will be a hard tree to climb – of this there is no doubt – but it will be the only one in the forest that bears fruit in a trade negotiation – that is certain.

In my book, I set out an analytical framework of economic and legal reasoning that can be applied to exclusionary business practices and draws from the experience and case law of both trade and competition policy. It focuses on seeking consensus, rather than compromise, between the two policy areas. It will not satisfy those who want unfettered access to all markets.

However, I hope that it can go a small way towards helping governments to introduce some true competition policy discipline into the world trading system... and I don't mind if that still doesn't happen in my lifetime, just as long as they get it right this time.

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