REDUCING GOVERNMENTAL IMPEDIMENTS TO CAPITAL MOBILITY

Remarks before the ASEAN Consultative Forum on Competition

Conference on "Competition Law and Policy: How to Make Competition Law and Policy Play a Greater Role In ASEAN Economies"

Bangkok
August 17, 2005

William Blumenthal[*]
General Counsel
Federal Trade Commission
Washington, D.C.

I am very pleased to have the opportunity to appear before you this morning. One of the issues on which ASEAN and its members have been working coincides with an interest that I have had for several years – namely, how to achieve the potential benefits of widespread competition law enforcement, while at the same time minimizing the harm that sometimes flows from the transnational effects of inconsistent or overextended enforcement practices.

In an article that I published last year before entering government service and while still a member of the private sector, I wrote:

> As international markets confront the jurisdictional reach of national competition authorities, the exercise of sovereign powers will spill across national borders. A decision by enforcement authorities in Country A may affect not only their own citizens, but also citizens in Country B. The respective effects are not necessarily the same. They may even be fundamentally inconsistent. As more competition regimes are adopted, implemented, and funded around the globe, and as more authorities assert extraterritorial application of their respective laws, the problem will likely increase.[1]

---

[*] These views are those of the author and do not necessarily represent the position of the Federal Trade Commission or of any individual Commissioner.

[1] William Blumenthal, *The Challenge of Sovereignty and the Mechanisms of Convergence*, 72 ANTITRUST L.J. 267, 267 (2004).

This concern was neither novel nor isolated. In a speech delivered in 2001, Tim Muris, then serving as Chairman of the agency at which I now work, expressed similar views:

> The spread of antitrust enforcement regimes has paralleled the increasing globalization of business activity over the past decade. Most countries in which multinational firms do business have a competition law and an enforcement agency.
>
> Businesses face different competitive conditions in the various countries in which they operate. Some of these differences arise from different legal and regulatory regimes that affect investment, employment, and taxation. Others arise from the market, such as distribution methods and their related costs, language, and customer tastes and preferences. As much as businesses strive for cost savings through, for example, the standardization of products and their distribution, to succeed they must accommodate the differences arising in those markets in which they participate.
>
> Just as competition conditions vary from country to country, so too do competition regimes. In many cases, the U.S. antitrust agencies work with foreign antitrust agencies whose laws – and, in some cases, enforcement goals – differ from ours. How enforcers manage those differences influences whether they achieve their enforcement goals; it also influences whether companies get caught in a multi-jurisdictional tug-of-war.[2]

My objective today is to build on these earlier discussions, with a particular focus on some relationships among competition policy, government-imposed restraints, capital flows, and incentives for investment and development. I will begin with the familiar issue of competition advocacy directed against traditional governmental restraints. I will then turn to restraints that are sometimes imposed by competition authorities themselves, with special attention paid to missteps in the areas of dominance, essential facilities, and merger process. As you will see, the missteps I have in mind are ones that tend to discourage investment and capital formation. Looking more closely at the merger process, I want to highlight some remedial measures that have been advanced by the world's competition law community through the work of the International Competition Network. Finally, in closing, I would like to offer some thoughts on the role that ASEAN and ACFC might play in the future as vehicles for useful regional cooperation.

---

[2] Timothy J. Muris, Chairman, Federal Trade Commission, *Merger Enforcement in a World of Multiple Arbiters*, Remarks before Brookings Institution Roundtable on Trade and Investment Policy (Dec. 21, 2001), available at http://www.ftc.gov/speeches/muris/brookings.pdf.

I. COMPETITION ADVOCACY AND GOVERNMENTAL

Article 86 of the Treaty limits the powers of the Member States to enact measures adversely affecting competition, and Article

States have now had more than a century of experience with administering our antitrust laws, and our practices have varied widely over that period. In retrospect, it is now clear that many of our practices in the middle of the last century were ill-considered, at least to the extent that efficiency and consumer welfare are to be treated as touchstones of sound competition policy.

Without attempting to be comprehensive, one can identify numerous practices that may initially sound reasonable, but that on inspection tend to suppress competition or discourage investment or both:

> Excessive skepticism towards horizontal restraints may discourage efficiency-enhancing joint ventures;
> Prohibition of vertical non-price restraints may prevent the adoption of efficient distribution systems;
> Prohibition of exclusive contracts or long-term contracts may limit the ability of

policies. The first and most important principle is that United States competition law does not condemn the mere possession of monopoly power, but punishes only misuse that results in a substantial injury to competition. In our view, punishment of a firm that obtains a dominant or monopoly position by reducing price or offering new or improved products or services is contrary to the goal of promoting comp

In the United States, our competition law does not limit the price that a monopolist is permitted to charge – a monopolist may charge as high a price as the market will tolerate. In our view, condemnation of monopoly pricing would discourage innovation and entry by new competitors. Risky investments in innovation are undertaken because of the prospect of a large payoff from a major technological breakthrough or a popular new consumer product. To punish the monopolist from receiving the payoff would deny the expected rewards of its success and would reduce the incentive to innovate and invest.

Unless the monopolist's market is characterized by barriers to entry (as that term is used in the economic sense), high prices normally will attract firms to enter the market, especially where the new entrant can offer a lower price, a better product, or enhanced services. The new entry will restore the competitive equilibrium, tending to drive prices back toward competitive levels without the need for government interference. If artificially elevated prices do not attract new entry, it may be appropriate to inquire into the reason that market forces are failing to respond. We have found that some of the most common and effective impediments to entry are anticompetitive regulatory barriers, which in principle should be within the government's own control.

Relying on market forces rather than enforcement will avoid imposing on competition officials the difficult, if not im

2. Compulsory Access

As we survey jurisdictions around the globe, we have seen a recent and renewed interest in a particular form of intervention that is sometimes urged as a possible remedy for dominant firms – namely, compulsory access to their so-called "essential facilities." We in the United States have developed substantial misgivings about intervention in this form, largely because of the adverse effects that I would like to describe here.

In our view, legal provisions on refusal of access to networks, infrastructure, and other "essential facilities" often harm procompetitive behavior, innovation, and effective protection for intellectual property rights. In the United States, our competition law generally does not restrict the right of a firm, including a monopolist, to exercise its independent discretion as to the parties with whom it will deal. Even firms with market power are permitted to refuse to deal with rivals. To require otherwise would chill the firms' incentives to innovate, invest, and compete.

Consider the analysis of a compulsory access from the perspective of a potential investor. If the investor commits funds and the investment fails, it absorbs the entire loss; it does not receive any subsidy from its competitors. But if the investor commits funds and the investment succeeds, it must now share the benefits with its competitors. An asymmetrical system of this type discourages entrepreneurial risk-taking, encourages free-riding, and becomes what one of our commentators has called "an insurance policy for laggards." To assure that investment and innovation are not discouraged, competitors must be confident in advance that they will not be required to share their successful assets with competitors. And to the extent that a legal system contemplates that mandatory sharing may be required in some instances, it will be important to minimize the disincentive for innovation and investment by providing sufficient detail to enable competitors to recognize in advance when the sharing obligations will be imposed.

Compulsory access to a network or other infrastructure presents another problem – it chronically leads to disputes on the terms of access, especially price, and resolving those disputes often entails intervention by agencies or courts. Compulsory access provisions tend to anticipate some form of cost-based regulation, which is inappropriate for risky investments. If investors are allowed to recover merely their costs when they succeed, they will lose the incentive to take risks. Even if a risk premium is allowed, investment incentives will still be distorted. Regulating non-price terms of access is also complex and may undermine the efficient utilization of facilities. In practice, compelling access to a network or other infrastructure requires the creation of mechanisms that will be needed to regulate the price and non-price terms of access and to monitor compliance. As we note above in connection with the objective of setting a "fair price," we have found that mechanisms of this type are generally beyond the capabilities of competition authorities. Most commentators agree that they are generally beyond the capabilities of the courts as well.

Some courts in the United States have articulated a so-called "essential facilities doctrine" under Section 2 of the Sherman Act to define exceptional circumstances in

which a duty to assist competitors may be found. In these cases, the courts have required the facility to be truly "essential," not mere

officials always continue to debate policy nuances – both within any given jurisdiction and across jurisdictions. As a practical matter, however, these sources of potential substantive dispute result in frictions in only sporadic cases. While the international competition community would benefit from the development of better mechanisms for averting or resolving those frictions,[13] the need does not seem to be urgent.

By contrast, we view the problems of global merger process as pressing.

In understanding the basis for this view, we should start with some rough statistics. More than seventy jurisdictions around the globe now have some form of merger review. Most of the merger review regimes provide for extraterritorial application, and even mergers between two foreign companies are subject to local notification obligations if the parties satisfy the regime's nexus requirements. /TTwe vif0.0e7.98dM0.00.000

capital, labor, or anything else that affects a firm's fortune. Sale of the company as a going business may cause minimum disruption to owners, managers, suppliers, customers, employees, and communities. To facilitate exit when it is desired may indeed facilitate entry. The likelihood of exit with minimum loss or maximum gain increases the attractiveness and reduces the risk of entering a market."

A. Nexus to the Reviewing Jurisdiction

The ICN's first Recommended Practice (Nexus to Reviewing Jurisdiction) provides that each jurisdiction's merger review rules should seek to screen out transactions that do not have an appreciable effect on competition within the jurisdiction. Merger control should cover only transactions that have an "appropriate nexus with the jurisdiction concerned." The rationale: Requiring notification of transactions that do not meet an appropriate standard of materiality as to the level of "local nexus" imposes unnecessary transaction costs on parties and consumes agency resources without any corresponding enforcement benefit. Accordingly, the Practice provides that notification of a transaction should not be required unless the transaction is likely to have a significant, direct, and immediate economic effect in the jurisdiction concerned.

Experience demonstrates that thresholds based on significant local sales or asset levels within the jurisdiction concerned are most suitable, and the Recommended Practice identifies these two factors as appropriate determinants of materiality. The Recommended Practice is silent as to the appropriate level at which to set such thresholds, because this will differ by jurisdiction. In the United States, for a transaction between foreign entities to be notifiable under our Hart-Scott-Rodino premerger notification filing requirement, the parties must have combined U.S. sales or assets exceeding US $116.8 million, and the acquired party must have assets or sales in or into the U.S. exceeding US $53.1 million.[17] The EU, by contrast, uses a higher primary threshold (each of at least two parties must have EU sales exceeding €250 million), in part because its system is designed to channel smaller transactions to Member States.

The question of the level at which a jurisdiction should set its thresholds will be taken up by the ICN next Spring through a workshop intended to promote greater understanding and implementation of the Recommended Practices. The workshop is still being designed, but it is currently envisioned as a two-day, interactive program intended for officials responsible for merger enforcement policy or premerger notification or both. Key aspects of the Recommended Practices, including how to set appropriate levels for thresholds that protect the public without unnecessarily burdening transactions that have only a limited relationship to the jurisdiction, will be addressed through panel discussions and hands-on breakout sessions. The workshop is likely to be held in Washington DC toward the end of March 2006.

The examples of thresholds from the U.S. and EU illustrate another key component of the ICN's jurisdictional nexus Practice: they measure nexus by reference to the activities of at least two parties to the transaction in the local territory and/or by reference to the activities of the acquired business in the local territory. The Recommended Practice notes that many jurisdictions require significant local activities by each of at least two parties to the transaction before the nexus requirement is satisfied; this is viewed as an appropriate local nexus screen.

---

[17] The U.S. thresholds are not round numbers because the statute provides for adjustments from the original values of $100 million and $50 million to reflect currency inflation.

With respect to transactions involving only one party with appropriate nexus to the jurisdiction, the Recommended Practice observes that the risk of competitive harm is sufficiently remote that the burden associated with notification is normally not necessary. The Recommended Practice further provides that if local nexus requirements are to be based on a single party, the requirements should (i) focus on the activities of the acquired business and (ii) use thresholds that are sufficiently high to avoid notification of transactions without potential material effect on the local economy.

The Recommended Practice states that notification should not be required solely by reference to the acquiring firm's local activities – for example, by reference to a local sales or assets test that can be satisfied by the acquiring person alone. Otherwise, notification would be likely to impose unnecessary transaction costs on a large number of transactions that do not pose any risk to competition in the jurisdiction. The Recommended Practices include a narrow exception (I.C comment 4) that was crafted to address special situations in certain small economies, but the exception is unlikely to apply to ASEAN member countries.

B. Notification Thresholds

With the burgeoning number of merger notification regimes worldwide, it is critical that each jurisdiction employ notification thresholds that are clear, understandable, and based on objectively quantifiable criteria. The ICN's second Recommended Practice (Notification Thresholds) notes that the efficient operation of capital markets is best served by such bright-line tests, which are more easily administrable by both agencies and parties.

The Recommended Practice identifies assets and sales as its two examples of objectively quantifiable notification criteria. All major jurisdictions with mandatory premerger notification currently conform to the recommendation or have made significant efforts to change their systems so as to conform.

The Recommended Practice explicitly states that thresholds based on market shares are inappropriate at the notification stage because they are not objectively quantifiable. Market share thresholds are extremely difficult for both the parties and the agencies to apply. They require significant amounts of data in order to define the relevant market, determine its overall size, and calculate the percentage attributable to each competitor. Market share determinations may be appropriate at a later, more substantive stage of the merger review, but our experience and the Recommended Practice dictate that they should be avoided for purposes of merger notification thresholds.

Similarly, a threshold requirement based on the portion of the value of a transaction attributable to the jurisdiction is too subjective or arbitrary to be an appropriate notification requirement. In the context of a multi-jurisdictional transaction, the parties generally will not have made such allocations prior to the time at which they must determine where to file notification. If such allocations are eventually needed for

commercial reasons, they will require complex modeling and often tax and accounting judgments that cannot reasonably be expected at the notification stage.

C. Review Periods

With the increasingly frequent experience of numerous jurisdictions reviewing the same transaction, the ICN's fourth Recommended Practice (Review Periods) recognizes the importance of review timetables based on reasonable, yet flexible periods. The Recommended Practice reflects parallel judgments: (a) that capital markets and related business interests are better served by avoiding unnecessary delays to closing and (b) that

grant early termination of applicable waiting periods, once the agency determines that the proposed transaction does not raise material competitive concerns.[18] This flexibility can be important to merging parties to guard against the deterioration of assets and to ensure that the merger's benefits are realized without undue delay or burden.

D. Requirements for Initial Notification

Flexibility is also important with respect to requirements for initial notification. The ICN's fourth Recommended Practice (Requirements for Initial Notification) recognizes that the duty to notify applies to transactions covering a wide range of possible competitive effects and that no single set of initial notification requirements will be optimal for all transactions. The Practice states, however, that because most transactions do not raise material competitive concerns, the initial notification should elicit the minimum amount of information necessary to initiate the merger review process by verifying that the transaction exceeds jurisdictional thresholds and determining whether the transaction raises competitive issues meriting further investigation.

The amount of information required will vary depending on the approach to notification thresholds taken by the jurisdiction. The Recommended Practice cautions jurisdictions that review a large number of transactions (due to low jurisdictional thresholds) to be particularly sensitive to disproportionate burdens arising from the breadth of their initial filing requirements. The United States, which receives between ewai 0 0 192 90 488.16 Tm( )TjETautMC /P <</MCID 9 >>BDC B5nge of

competition concerns. Flexibility of this type has proven to be valuable in averting significant burdens both for parties (with respect to the time and cost of compiling such information for transactions that do not raise competitive concerns) and for enforcers (with respect to the need to devote resources sorting through information unnecessarily compelled from the parties).

CONCLUDING REMARKS

At the beginning of my remarks this morning, I referred to an article I published last year on the potential for inconsistency and burden in a world where many competition authorities apply their sovereign powers on an extraterritorial basis. Surveying the literature, the article identified four approaches that commentators have advanced as a possible remedy:

> urge that we spend a large part of our cooperation/convergence efforts in building and strengthening these regional networks under the larger ICN umbrella. Countries within regions are united by common geography and often a common language and they are often at similar stages of economic development and therefore face similar competition problems. Working together, they should be able to pool resources to provide more support and assistance to one another in enforcing their laws and in building a strong competition culture in their region.[22]

An approach of regional cooperation is subject to certain important limitations.[23] In conjunction with other approaches, though, it offers promise