

INDIVIDUAL EXEMPTIONS AND THE STRATEGIC THREAT OF EXIT: THE CASE OF AIRLINE JOINT SERVICE AGREEMENTS

Abstract

by Cecil Duncan MacRae & Elizabeth Chase MacRae*

One of the strategic forms of interaction between firms and competition authorities is the threat, explicit or implicit, by firms to exit the particular market in which the authority is enforcing the competition law. By threatening to exit the market, the firms threaten to reduce the consumer welfare or total welfare in the market, which the authority values. Multinational firms may even threaten to exit the jurisdiction of the authority if the national competition law, or enforcement of the national law by the authority, is not favorable to these firms. This interaction is, in principle, not dissimilar to the interaction between multinational firms and fiscal or regulatory authorities. The firm threatens to leave the economy of the authority if the national fiscal or regulatory environment is not attractive to the firm.

The strategic threat of exit from a market in which the competition law is being enforced is relevant for all competition authorities. All authorities care about the consumer welfare or total welfare in their markets. The threat to exit the jurisdiction is also relevant, in principle, for all competition authorities. This threat is particularly relevant for a competition authority in an open economy not subject to a supra-national competition authority, such as exists in the European Union (EU). However, the strategic threat of exit is also relevant for national competition authorities in the EU if the antitrust-related activities of the firm fall outside the scope of the supra-national authority. The threat of exit is even relevant for a supra-national authority if the threat is to leave the jurisdiction of the supra-national authority.

One area of antitrust where the strategic threat of exit is especially relevant is in the granting or denial of individual exemptions. In response to the termination of an existing exemption, or the denial of a request for a new exemption, by a national competition authority, a firm affected by the exemption can threaten to leave a market of the authority or to leave or not come to the jurisdiction of the authority. For example, a competition authority deciding whether or not to have an individual exemption for certain airline alliance agreements will consider whether the airlines will cease providing service to certain markets in the nation, or avoid using the nation as a transit point if the exemption is not allowed.

The purpose of this paper is to analyze the strategic interaction between firm and competition authority in the context of individual exemptions for certain airline alliance agreements. We begin by developing a bargaining theory model of individual exemptions with exit. We then apply the model to individual exemptions for airline joint service agreements. We devote particular attention to the recent decisions on airline joint service agreements by the competition authorities in Australia and Singapore.

* C.D. MacRae is on the faculty of the School of Law at the Singapore Management University (SMU) and E.C. MacRae is on the faculty of the Lee Kong Chian School of Business at SMU.