Dimensions of strategic behaviour to the competition law: some Dutch experiences

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Abstract

It is well known that the Sherman Act of 1890 led to strategic behaviour by firms. Because cartels were forbidden by law, the number of mergers increased in the US. Especially after 1897 there was a clear and big increase in the number of mergers (Motta, 2004, pp. 5). This lead to the Clayton Act of 1914 which established a legal foundation for merger control in the US.

These historical observations illustrate two points. First, the market reacts to institutional changes like changes in legislation. Secondly, the legislator has a tendency to react to a new situation with amendments to the existing competition law.

When competition legislation is introduced or amended in order to achieve a policy goal – which is generally supposed to be in the interest of the public- firms try to implement the law at the lowest cost and with a maximum of advantage. This process might lead to an implementation of the law, but also in some cases to an evasion or to something in between. However, it may take some time before this adoption process is fully settled down. This might explain why it took more than half a decade before the market reacted to the Sherman Act. In a recent study by the Netherlands Bureau for Economic Policy Analyses (CPB) it is argued that in the period 1994-2001 the reaction to a change in the market circumstances, legislation, and market demand etc., took about two years:

> "The size of the coefficient of the lagged indicator suggests an adjustment of firms' competitive behaviour to changes in the other determinants in the previous year. The coefficient of 0.44 implicates that competition is fully adjusted tot initial changes of other determinants after two years."(CPB (2006), p. 37)

So, changes in the law lead to reactions of economic agents but it takes time. This adoption process leads to a new equilibrium. In this equilibrium it is possible that the new law is fully implemented, but it is also possible that it is partly absorbed with evasive behaviour.

The legislative response to changes in market behaviour starts a process of action-reaction between the legislator and the market. This process runs the risk that an overdose of legislation and regulation is created as the legislator keeps adjusting the law to reach a perfect outcome.

The competition law of The Netherlands dates from 1998. It is essentially the same legislation as EU competition law. The law of 1998 substituted the law of 1956 called the WEM (Wet Economische Mededinging) which allowed trust agreements as long as they were reported to the Ministry of Economic Affairs. From the start of the EU, competition law has been operative (though rigorously applied since the 1990's only). Since this law was stricter than the Dutch WEM, a lot of Dutch competition cases in the period before 1998 were based on

this EU law rather than on the WEM and handled by the European Commission rather than Dutch authorities.

Until recently in the Netherlands there were hardly any changes in the competition law of 1998, but at this moment the first major changes in the law are in preparation, due to (for some part) certain market developments.

Economically induced reactions to a change in the law do not have to be illegal. An evasion of the competition law is a form of moral hazard which in itself does not have to be unlawful. The problem with moral hazard is that a response of the legislator will increase the administrative burden in due course. Another problem may be that it leads to inefficient behaviour or choices of the firms themselves. This administrative burden of legislation is one of the reasons why markets often do not function properly. In the end it is a question of balance between an increase in administrative burden and acceptance by policy makers that some moral hazard always is there.

Therefore the process of legislation and all kinds of rules also calls for reconsideration of the law now and again. Regulation runs the risk of becoming obsolete. On the one hand it is necessary to update legislation which can then be enforced. On the other hand competition policy which becomes too complicated because of regular adjustments will hamper the functioning of markets[1]. This is the paradox of competition policy.

Apart from adapting to changes in law, there are also other kinds of reactions by market parties to existing competition law, competition authorities, the (competition) regulators and (private and public) law enforcement agencies.

In this paper we will dwell on the effect of legislation on the administrative burden and on possible reactions of market parties to competition authorities, to each other and to competition law in general. We will dig into the problem of how parties try to influence one and another and the competition authority and how this competition authority should react to that.

Outline of the paper

First, we give some considerations on the trade-off between competition policy legislation and the reaction of economic agents. What should the proper reaction (function) of legislators be towards the administrative burden of law enforcement and monitoring of competition policy?

Secondly (and related), we will consider the reaction of competitors to each other. There are examples of companies which sue other companies or try to draw the competition authority's attention for a case or to try to harm competitors. It might sometimes also be a way of attracting public attention to a specific interest which might mobilise the public opinion. We

[1] The study of the CPB warns for "a trade-off between the aim to increase competition and to reduce the administrative burden for firms. On the one hand, policy wants to reduce the administrative burden for firms…on the other hand, policy tries to stimulate competition and wants to have the opportunity to monitor and evaluate their competition measures." (CPB (2006), p. 46).

give a summary of the arguments which can be drawn from the literature in this respect. We provide a number of Dutch examples.

Thirdly, we describe the relation relation between the competition authority and the economic agents which are the subject of the enforcement of competition policy and regulation. Here we also give an overview of the literature. We find that most of the literature on this subject is about the relationship between competition regulators and privatized sectors such as telecommunication, railroads, electricity etc. Again we give Dutch examples.

Beside this direct relationship between companies and the competition authority there is also an exposure effect of merger control and law enforcement of the competition law. In the second part of the paper we present a recent research on the anticipated effects of companies on the Netherlands competition authority. This longitudinal research shows that companies increasingly take the competition law and the competition law enforcement into account in their business decisions with regard to mergers. There are however substantial differences between industries.

We conclude with some suggestions for a code of conduct between companies and authorities.

Literature:

M. Motta, *Competition Policy: Theory and Practice*, Cambridge University Press, Cambridge, 2004

Creusen, H., B. Minne and H. van der Wiel, *Competition en the Netherlands*, CPB Document, no.136, The Hague, December, 2006