

# Entrepreneurship and the EU Competition Law Deterrence Paradox

Prepared for the 6<sup>th</sup> Annual ACLE Competition and Regulation Meeting, 22<sup>nd</sup> April 2010,  
Amsterdam, The Netherlands,

work in progress

Patricija Kotnik and Mitja Kováč

University of Ljubljana, Faculty of Economics, Kardeljeva ploscad 17, 1000 Ljubljana  
e-mail: [patricija.kotnik@ef.uni-lj.si](mailto:patricija.kotnik@ef.uni-lj.si), [mitja.kovac@ef.uni-lj.si](mailto:mitja.kovac@ef.uni-lj.si)

---

Abstract:

The efficient regulatory mechanisms inducing innovation, cooperation and deterring competition law infringements have recently been the subject of an increasing attention and intense scholarly debate. Competition is essential to the innovation process which in general terms enables entrepreneurship. But so is the cooperation between firms which requires disclosure of information and which may lead to the inefficient collusive behavior. Providing incentives for technological innovation (spurring the generation and utilization of productive information), entrepreneurship and cooperation, and deterring opportunism are of the essential importance for economic growth and maximization of social welfare. Yet, the related optimal trade-off between the provision of stable and optimal entrepreneurial incentives and the related EU competition law infringements has been largely exempted from the current scholarly debate. Hence, the challenge for the optimal regulation policy is to find the right balance between those seemingly conflicting issues and policies. This paper offers an economic evaluation of optimal entrepreneurial incentive mechanisms and provides a behavioral and traditional law and economics' arguments for an optimal regulatory respond.

The main propositions and conclusions are the following: (1) In principle, the least cost information gatherer should produce and communicate information. (2) There should be no duty to reveal entrepreneurial information. (3) Current EU competition law enforcement (market share criterion) deters the utilization of deliberately acquired productive information and thus hinders innovation and entrepreneurial activity. (4) Voluntary productive information sharing should be induced, whereas the sharing of redistributive information between firms should be deterred. (5) Less is more: parties get better informed when unimportant information is filtered away. (6) The identified expected benefits from certain marginal entrepreneurial activity may well, under the current EU enforcement regime, be outweighed by the inefficient risk shifting and increased transaction costs assigned upon entrepreneur. This in effect hinders the optimal level of entrepreneurial activity and may be a source of stark inefficiencies (diminishing social welfare).

**JEL classification:** K42.

**Keywords:** Regulation law and economics, entrepreneurship, efficiency, information, competition.

## References

- Akerlof, A. George, The Market for Lemons: Qualitative Uncertainty and the Market Mechanism, 84 Quarterly Journal of Economics 488, 1970.
- Atiyah, P.S., Smith, A. Stephen, Atiyah's Introduction to the Law of Contract, Clarendon Press Oxford, 2005.
- Beale, Hugh, Hartkamp, Arthur, Kotz Hein and Tallon Denis, Contract Law: Cases, Materials and text, Hart Publishing, 2002.
- Barnett, E. Randy, Rational Bargaining Theory and Contract: Default Rules, Hypothetical Consent, The Duty to Disclose, and Fraud, 15 Harv. J.L. & Pub. Pol'y 783, 1992.
- Bartels, Martin, Contractual Adaptation and Conflict Resolution, Studies in Transnational Law of Natural Resources, Volume 8, Kluwer Law and Taxation Publishers, Deventer, 1985.
- Beatson, Jack, Friedmann, Daniel (eds.), Good Faith and Fault in Contract Law, Clarendon Press, Oxford, 1995.
- Beatson, J., Anson's Law of Contract, 28<sup>th</sup> ed., Oxford University Press, 2002.
- Bebchuk, Arye Lucian, Ben-Shahar, Omri, Precontractual Reliance, 30 J. Legal Stud. 423, 2001.
- Birmingham, L. Robert, The Duty to Disclose and the Prisoner's Dilemma: Laidlaw v. Organ, 29 WM. & Mary L. Rev. 249, 1988.
- Bishop, S., Walker, M., The Economics of EC Competition Law: Concepts, Application and Measurements, Sweet & Maxwell, 2002.
- Buccirossi, Paolo (ed.), Handbook of Antitrust Economics, The MIT Press, 2008.
- Carlton, W. Dennis, Fischel, R. Daniel, The Regulation of Insider Trading, 35 Stan. L. Rev. 857.
- Coleman, L. Jules et al., A Bargaining Theory Approach to Default Provisions and Disclosure Rules in Contract Law, 12 HARV.J.L.&PUB. POL'Y 639, 1989.
- Cooter, Robert and Thomas Ulen, Law and Economics, Addison Wesley Longman, 4th Edition, 2004.
- Craswell, Richard, Contract Law: General Theories, in Bouckaert, Boudewijn and De Geest, Gerrit (eds.), Encyclopedia of Law and Economics, 1999.
- Craswell, Richard and Alan Schwartz, Foundations of Contract Law, Foundation Press, 1994.
- Curran, Christopher and David Haddock, An Economic Theory of Comparative Negligence, 14 Journal of Legal Studies 49, 1985.
- Curnes, J. Ellen, Protecting the Virginia Homebuyer: A Duty to Disclose Defects, 73 Va. L. Rev. 459, 1987.
- De Geest, Gerrit, Economische analyse van het contracten- en quasi-contractenrecht, Antwerpen, MAKLU, 1994.
- De Geest, Gerrit, Jacques Siegers and Roger Van Den Berg (eds.), Law and Economics and the Labour Market, New Horizons in Law and Economics, Edward Elgar, 1999.
- De Geest, Gerrit, Teun, Jaspers, Jacques, Siegers and Ann-Sophie, Vandenberghe, *The right to lie: new law and economics versus Dutch labour law?*, in De Geest, Gerrit,

- Jacques Siegers and Roger Van Den Berg (eds.), *Law and Economics and the Labour Market*, New Horizons in Law and Economics, Edward Elgar, 1999.
- De Geest, Gerrit, *Comparative Law and Economics and the Design of Optimal Doctrines*, in Deffains, Bruno and Kirat, Thierry (eds.), *Law and Economics in Civil Law Countries*, New York, JAI (Elsevier), 107-124, 2001.
- De Geest, Gerrit, *The Signing-Without-Reading Problem: An Analysis of the European Directive on Unfair Contract Terms*, in Schäfer, Hans-Bernd and Lwowski, Hans-Jürgen (eds.), *Konsequenzen wirtschaftsrechtlicher Normen*, 213-235, 2002.
- De Geest, Gerrit, *Economic Analysis of Commercial and Labour Contracts*, Utrecht University, unpublished manuscript, 2003.
- DeMott, A. Deborah, Do you have the Right to Remain Silent?: Duties of Disclosure in Business Transactions, 19 Del. J. Corp. L. 65, 1994.
- Eisenberg, A. Melvin, Disclosure in Contract Law, 91 Cal. L. Rev. 1645, 2003.
- Epstein, R., Behavioral Economics: Human Errors and Market Corrections. The University of Chicago Law Review, 73, 111-131, 2006.
- Fabre-Magnan, Muriel, Duties of Disclosure and French Contract Law, in Beatson, Jack and Friedman, Daniel (eds), "Good Faith and Fault in Contract Law," Clarendon Press Oxford, 99-123, 1995.
- Farrell, J., Voluntary Disclosure: Robustness of the Unraveling Result, and Comments on Its Importance, in R. Grieson (ed.), *Antitrust and Regulation*, Lexington books, 1986.
- Flume, Werner, *Allgemeiner Teil des Bürgerlichen Rechts, Das Rechtsgeschäft*, 3<sup>rd</sup> Edition, Berlin-Heidelberg-Nova Lorque, 1979
- Fishman, J. Michael, Hagerty, M. Kathleen, The Optimal Amount of Discretion to Allow in Disclosure, 104 Quarterly J. Econ. 427, 1990.
- Foulke, R. Roland, Mistake and the Formation and Performance of a Contract, 11 Colum. L. Rev. 197, 1911.
- Frug, J. Mary, Rescuing Impossibility Doctrine: A Postmodern Feminist Analysis of Contract Law, 140 U. Pe. L. Rev. 1029, 1992.
- Fuller, F. Hoffman, Mistake and Error in the Law of Contracts, 33 Emory L.J. 41, 1984.
- Ghestin, Jacques, The Pre-contractual Obligation to Disclose Information, 1: French Report, in Harris and Tallon (eds.), *Contract Law Today, Anglo-French Comparisons*, Oxford, 1989.
- Giliker, Paula, *Pre-contractual Liability in English and French Law*, Kluwer Law International, 2002.
- Giliker, Paula, Regulating Contracting Behaviour: The Duty to Disclose in English and French Law, 5 European Review of Private Law 621-640, 2005.
- Goyder, D.G., *EC Competition Law*, 4<sup>th</sup> ed., Oxford University Press, 2003.
- Gordley, James, Mistake in Contract Formation, 52 Am. J. Comp. L. 433, 2004.
- Gordley, James and Von Mehren, A. Taylor, *An introduction to the Comparative Study of Private Law: Readings, Cases, Materials*, Cambridge University Press, 2006.
- Grosskopf, Ofer, Medina, Barak, Why Do We Know What We Know? Reevaluating the Economic Case against Pre-Contractual Disclosure Duties and for Break-up Fees, SSRN Working Paper Series, September 1, 2006, available at: <http://ssrn.com/abstract=935165>
- Grossman, J. Sanford, The Informational Role of Warranties and Private Disclosure about Product Quality, *Journal of Law and Economics*, Vol. XXIV, 461-489, 1981.

- Guth, W., Schmittberger, R., and Schwartz, B., An experimental analysis of ultimatum bargaining, *J.E.B.O.* 3, 367, 1982.
- Harris, Donald and Tallon, Denis (Eds.), *Contract Law Today, Anglo-French Comparisons*, Clarendon Press Oxford, 1989.
- Hirschleifer, Jack, The Private and Social Value of Information and the Reward to Inventive Activity, *61 Am. Econ. Rev.* 561, 1971.
- Jolls, J., Sunstein, C. R., & Thaler, H. R., A Behavioral Approach to Law and Economics. *Stanford Law Review*, 50, 559-606, 1998.
- Jolls, J., Behavioral Law and Economics. In P. Diamond & H. Vartainen (Eds.). *Behavioral Economics and its Application*. Princeton University Press, 2007.
- Jones, Alison, Sufrin, Brenda, *EC Competition Law: Text , Cases and Materials*, 3<sup>rd</sup> ed., Oxford University Press, 2008.
- Jovanovic, Boyan, Thrutful Disclosure of Information, *Bell Journal of Economics*, Vol. 13, 36-44, 1982.
- Kaplow, Louis, Shapiro, Carl, Antitrust, in Polinsky, A. Mitchell, Shavell, Steven (eds.) *Handbook of Law and Economics – Vol II.*, North-Holland, 2009.
- Keeton, W. Page, Fraud-Concealment and Non-Disclosure, *15 Tex. L. Rev.* 1, 25, 1936.
- Kötz, Hein, Flessner Axel, *European Contract Law: Formation, Validity and Content of Contracts; Contract and Third Parties*, Clarendon Press Oxford, 1997.
- Kötz, Hein, Precontractual Duties of Disclosure: A Comparative and Economic Perspective, *European Journal of Law and Economics*, 9:5-19, 2000.
- Krawiec, D. Kimberly, Zeiler, Kathryn, Common Law Disclosure Duties and the Sin of Omission: Testing the Meta-theories, Social Science Research Network Paper, November 2004, downloadable at: <http://ssrn.com/abstract=614501>
- Kronman, T. Anthony, Mistake, Disclosure, Information, and the Law of Contracts, *Journal of Legal Studies*, Vol. 7, 1-34 (1978)
- Kull, Andrew, Mistake, Frustration, and the Windfall Principle of Contractual Remedies, *43 Hastings Law J.* 1, 1991.
- Kull, Andrew, Unilateral Mistake: The Baseball Card Case, *70 Wash. U. L. Q.* 57, 1992.
- Landes, M. William and Richard A. Posner, *The Economic Structure of Tort Law*, Cambridge (MA): Harvard University Press, 1987
- Lando, Ole, Principles of European contract law and Unidroit principles-Similarities, Differences and Perspectives , *Centro di studi e ricerche di diritto comparato e straniero*, Roma 2002.
- Lando, Ole, *The Principles of European Contract law, Dordrecht [etc.] : Nijhoff [etc.]*, 1995-2003.
- Legrand, Pierre, Pre-contractual Disclosure and Information: English and French Law Compared, *6 Oxford Journal of Legal Studies* 322, 1986.
- Legrand, Pierre, Information in formation of contracts: a civilian perspective, in *Essays in Honour of Jacob S. Ziegel*, *19 Can. Business. L. J.* 318, 1991.
- Levmore, Saul, Securities and Secrets: Insider Trading and the Law of Contracts, *68 Va. L. Rev.* 117, 1981.
- Lyons, Bruce (ed.), *Cases in European Competition Policy: The Economic Analysis*, Cambridge University Press, 2009.
- Lundström, Anders, Stevenson, A. Lois, *Entrepreneurship Policy – Theory and Practice*, Springer 2005.

- Mackaay, Ejan, *Economics of Information and Law*, Kluwer Nijhoff Publishing, 1982.
- Mahoney, G. Paul, *Contract Remedies: General*, in Bouckaert, Boudewijn and De Geest, Gerrit (eds.), *Encyclopedia of Law and Economics*, Edward Elgar Inc., 1999.
- Malerba, Franco, Brusoni, Stefano, *Perspectives on Innovation*, Cambridge University Press, 2007.
- Marshall. M. John, *Private Incentives and Public Information*, 64 *Am. Econ. Rev.* 561, 1974.
- Matthews, Steve and Andrew Postlewaite, *Quality Testing and Disclosure*, *The RAND Journal of Economics*, Vol.16, No.3, 328-340, 1985.
- McMullen, S. Jeffery, Bagby, D. Ray, Palich, E. Leslie, *Economic Freedom and the Motivation to Engage in Entrepreneurial Action*, Baylor University Press, 2008.
- Milgrom, P.R., *Good News and Bad News: Representation Theorems and Applications*, *Bell Journal of Economics*, Vol. 12, 380-391, 1981.
- Minitti, Maria, *The Role of Government Policy on Entrepreneurial Activity: Productive, Unproductive, or Destructive?*, Baylor University Press, 2008.
- Narasimhan, Subha, *Of expectations, Incomplete Contracting and the Bargain Principle*, 74 *Cal. L. Rev.* 1134, 1986.
- Nicholas Barry, *The Pre-contractual Obligation to Disclose Information, 2: English Report*, in Harris and Tallon (eds.), *Contract Law Today, Anglo-French Comparisons*, Oxford, 1989.
- Okuno-Fujiwara, Mashiho, Andrew Postlewaite and Suzumura Kotaro, *Strategic Information Revelation*, *The Review of Economic Studies*, Vol. 57, 25-47, 1990.
- Palmieri, W., Nicola, *Good Faith Disclosures Required During Precontractual Negotiations*, 24 *Seton Hall L. Rev.* 70, 1993.
- Parker, C. Simon, *The Economics of Entrepreneurship*, Cambridge University Press, 2009.
- Posner, A. Richard, *Economic Analysis of Law*, Sixth Edition, Aspen Publishers, 2003.
- Rasmusen, Eric and Ian, Ayres, *Mutual and Unilateral Mistake in Contract Law*, *Journal of Legal Studies*, Vol.XXII, 309-345, 1993.
- Ruble, Richard, Versavel, Bruno, *Market Share, R&D Cooperation, and EU Competition Policy*, Emylon Business School working paper 2009/03, 2009.
- Rubin, H. Paul, *Information Regulation - Including Regulation of Advertising*, in Bouckaert, Boudewijn and De Geest, Gerrit (eds.), *Encyclopedia of Law and Economics*, 1999.
- Schäfer, Hans Bernd and Claus Ott, *Lehrbuch des ökonomischen Analyse des Zivilrechts*, 250-58, 1986.
- Schwartz, Alan, Wilde, L. Luis, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 *U. Pa. L. Rev.* 630, 1979.
- Sefton-Green, Ruth (ed.), *Mistake, Fraud and Duties to Inform in European Contract Law*, Cambridge University Press, 2005.
- Shavell, Steven, *Acquisition and Disclosure of Information Prior to Sale*, *The RAND Journal of Economics*, Vol. 25, No.1, 20-36, 1994.
- Shell, G. Richard, *Opportunism and Trust in the Negotiation of Commercial Contracts: Toward a new Cause of Action*, 44 *Vand. L. Rev.* 221, 1991.
- Simon, H. A., *Models of Bounded Rationality*. Cambridge MA: MIT Press, 1982.

- Smythe, D. James, The role of Contractual Enforcement and Excuse in the Governance of Relational Agreements: An Economic Analysis, *Global Jurist Frontiers* Vol. 2, No. 2, Article 3, 2002.
- Smith, Janet Kiholm and Richard L. Smith, Contract Law, Mutual Mistake, and Incentives to Produce and Disclose Information, *Journal of Legal Studies*, Vol. XIX, 467 – 488, 1990.
- Stigler, J. George, The Economics of Information, 69 *J. Pol. Econ.* 213, 1961.
- Strudler, Alan, Moral Complexity in the Law of Nondisclosure, 45 *UCLA L. Rev.* 337, 1997.
- Swartz, Alan, Relational Contracts in the Courts, 21 *J. Leg. Studies* 271, 1992.
- Trebilcock, J. Michael, *The Limits of Freedom of Contract*, Harvard University Press, 1993.
- Waddams, S.M., Pre-contractual Duties of Disclosure, in Cane, Peter and Stapleton Janne (eds.), *Essays for Patrick Atiyah*, Clarendon Press Oxford, 1991.
- Whiston, D. Michael, *Lectures on Antitrust Economics*, The MIT Press, 2008.
- Whish, Richard, *Competition Law*, 6<sup>th</sup> ed., Oxford University Press, 2003.
- Williamson, E. Olivier, *Markets and Hierarchies: Analysis and Antitrust Implications*, 4-7 (1975).
- Wonnell, T. Christopher, The Structure of a General Theory of Nondisclosure, 41 *Case W. Res. L. Rev.* 329, 1991.
- Zhou, Qi, Law and Economics of Fraudulent Misrepresentation, SSRN Working Paper Series, May 2006, available at: <http://ssrn.com/abstract=900145>