Can Competition Law Deal with Disruptive Digital Technologies in Developing Countries?

DR R. IAN MCEWIN - COMPETITION CONSULTING ASIA

2ND EAST ASIA ACADEMIC NETWORK ON COMPETITION POLICY (EANCP) CONFERENCE - UNSW 29 AUGUST 2018

Introduction

- The history of the introduction of competition law around the world has been one of mostly copying developed country laws. Most countries have made little attempt has been made to adapt competition laws to local circumstances.
- However, lawyers are trained to interpret laws and past decisions not to determine the impact on local economies. This makes lawyers particularly unsuited to designing and interpreting competition laws in developing countries particularly with new industries and markets like the new digital economy.
- The realities of local economies should prevail – which are best determined by economists, not lawyers. This is particularly important where the digital economy is concerned where the economics of new technologies and their effects are likely to be factually complex

Disruptive Digital Technologies

"The Commission anticipates digital technologies will continue and likely accelerate changes in Australia's economy. Digital technologies offer greater scope for more distributed production, and facilitate the trend toward more service elements — pre- and post-production services — in manufactured and other goods. Data is a new source of market power but, in the face of the digital economy, advantage may also only be short lived. How governments deal with market power will be important for both those who control, and those who want to use, data and networks."

"Digital Disruption: What do governments need to do?" Productivity Commission Research Paper June 2016, p. 2.

Disruptive Digital Technologies

- Traditional economy characterized by:
  - vertical value chains where each production and distribution level adds economic value
- Digital economy economic value is generated;
  - in complex and dynamic networks
  - data is critical and its collection:
    - generates new markets, e.g. by selling data sets to third parties
    - introduces new products into existing markets
- Competition implications include:
  - greater availability of information leads to greater transparency which could lead to increased collusion;
  - User-generated information may make consumer reservation price predictions more accurate which can lead to more precise price discrimination
  - dynamic cooperation and competition between platforms can lead to asymmetric information flows to consumers and thus make them more vulnerable to exploitation

Competition Law and Economic Growth and the Digital Economy

- For developing countries faced with high levels of poverty, lack of education and corrupt institutions, economic development and growth are priorities. Economic growth (a general increase in real output) results both from:
  - greater use of available resources (less unemployment and increases in natural resources) and
  - more productive resource use (from productivity improvements in human capital and technology).
- More productive resource use results from innovative actions.
  - For advanced economies this means technological product or process advancements.
  - For developing countries technological change mainly results from trade and foreign investment including education. Innovation mostly occurs by adapting the way overseas markets work to local conditions and changing organisational forms to improve productivity. Innovations may be disruptive if local markets are weak due to poor property rights protection, poor contract enforcement, lack of remedies against fraud and so on. Researching and prescribing competition laws or administering a legal regime appropriate to local conditions cannot be done within legal systems.
- Law and economics research is required where the impact is empirically assessed. In practice, lawyers operate within a legislative and judicial world, they mostly simply copy laws from other jurisdictions without considering the economic and social conditions in which they operate.

Economics is Important to Decisions

- Competition law judges must translate economic theory into legal issues or policy – judges will do this differently not only across countries but within a country
- Economic theory describes how markets work – but there are competing economic theories based on:
  - Assumptions about:
    - human rationality (rational versus behavioural economic etc.)
    - whether markets self-correct if possible anti-competitive conduct is allowed
  - Theory and **admitted evidence** about:
    - Impact of alleged anti-competitive conduct
    - Efficiency benefits and costs
- Countries differ in the extent to which:
  - They pursue economic goals
  - How they use economic theory (in particular assessing the social costs of alternate policies including direct regulation – including the digital economy)
  - Whether they understand how economic theory applies to their own economic circumstances
- So why copy decisions based on economics and institutions from other countries?
  - Where the economic facts are similar but likely to be different and
  - Where different standards of proof and admissibility may apply

Why Economics Should Motivate the Design and Operation of New Competition Laws

- Economics provides help with:
  - Interpreting goals of competition law (protecting competitive processes; promoting consumer or total welfare) – also useful in effectively promoting non-economic goals such as fairness, redistribution etc.
  - Interpreting legislation e.g. markets, market power, dominance, concerted practice, assessing competition,
  - Determining and establishing relevant facts and their probative value in cases
  - Predicting empirically the likely effect of conduct (on price, output, innovation etc)

The Error Cost Approach to Designing and Enforcing Competition Law Rules

- While it is appropriate to consider whether laws achieve their goals, the costs of the legal system including the likelihood of error also need to be considered.
- In new agencies in developing countries errors are more likely which can be costlier and harder to remedy than in developed countries. More so when the digital economy is considered. But developing countries have limited resources.
- Judge Frank Easterbrook introduced the error-cost approach to competition law in the early 1980s but little account of this evidence-based, cost-benefit approach seems to be taken in designing and enforcing competition laws in developing countries

ALDEN ABBOTT'S EIGHT PRINCIPLES

https://www.heritage.org/government-regulation/commentary/cost-benefit-framework-antitrust-enforcement-policy

1. Enforcers should seek to identify and **expound simple rules** they will follow in both case selection and evaluation of business conduct, in order to rein in administrative costs.
2. Following Easterbrook, place a **greater emphasize on avoiding false positives** than false negatives, particularly in the area of unilateral conduct (since false positives may send cautionary signals to third party businesses that the market cannot easily correct).
3. Pursue cases **based on hard empirically-based indications of likely anticompetitive harm**, rather than theoretical constructs that are hard to verify.
4. **Avoid behavioral remedies** in merger cases (and, indeed, other cases) to the greatest extent possible, given inherent problems of monitoring and administration posed by such requirements.
5. Emphasize giving **full consideration to efficiencies (including dynamic efficiencies**), given their importance to innovation and economic welfare gains.
6. Announce positions in **public pronouncements and guidelines that are as simple and straightforward as possible**. Agency guidance should be "tweaked" in light of compelling new empirical evidence, but "pendulum swing" changes should be minimized to avoid costly uncertainty.
7. In non per se matters, pledge that they **will only bring cases when (1) they have substantial evidence for the facts on which they rely and (2) that reasoning from those facts makes their prediction of harm to future competition more plausible than the defendant's alternative account of the future.**
8. For cartel conduct, adjust leniency and other enforcement policies **based on the latest empirical findings and economic theory, seeking to pursue optimal detection and deterrence in light of "real world" evidence**

Differing Economic Conditions

- Available data are not nearly as good as in developed countries and so competition law decisions in local conditions are unlikely to be made on the basis of sophisticated data analysis.
- Error costs are likely to be different and so different trade-offs between false convictions (Type I) and false acquittals (Type II) errors should follow. Markets for the same product or service will differ in different overseas markets.
- The slope of demand curves will reflect: preferences (which will differ considerably between countries); actual and potential product substitutes (which will differ according to local supply, the willingness of importers to buy, the presence of illegal markets etc)
- Movements in the demand curve will reflect dynamic competition in the market, innovation etc. Shifts in the supply curves will reflect changes in input prices, production innovation will lower costs and so the supply curve. These factors are likely to differ between countries – and the likelihood that markets will overcome anti-competitive practices and so competition law decisions to intervene.
- Overseas lawyers cannot understand the underlying economics and so cannot advise on anti-competitive economic effects. Instead they can only espouse the latest legal thinking on competition rules elsewhere.

Malaysian Competition Act 2010

"An Act to **promote economic development** by promoting and protecting the process of competition, thereby protecting the interests of consumers and to provide for matters connected therewith. WHEREAS **the process of competition encourages efficiency, innovation and entrepreneurship, which promotes competitive prices**, improvement in the quality of products and services and wider choices for consumers."

Section 4. (1) A horizontal or vertical agreement between enterprises is prohibited insofar as the agreement has **the object or effect** of significantly preventing, restricting or distorting competition in any market for goods or services.

(2) Without prejudice to the generality of subsection (1), a horizontal agreement between enterprises which has the object to— (a) fix, directly or indirectly, a purchase or selling price or any other trading conditions; (b) share market or sources of supply; (c) limit or control— (i) production; (ii) market outlets or market access; (iii) technical or technological development; or (iv) investment; or (d) perform an act of bid rigging, **is deemed to have the object** of significantly preventing, restricting, or distorting competition in any market for goods or services.

- Not a per se rule as in the U.S. rather a prohibition and basis for exemption (see s 5 Relief of Liability)

Malaysian Competition Act 2010

- Section 4 is modelled on EU Article 101 – but Malaysia adds the 'deeming' provision.
- EU case-law provides that "certain forms of coordination are, by their very nature, harmful to the proper functioning of normal competition"30 and "reveal sufficient degree of harm" (*Allianz Hungária Biztosító and Others v. Gazdasági Versenyhivatal 2013)* and so it"may not be necessary to examine their actual effects on competition" (*Competition Authority v Beef Industry Development Society (BIDS), 2008)* restriction of competition by 'object' must be interpreted strictly (*F. Hoffmann-La Roche Ltd and Others v Autorità Garante della Concorrenza e del Mercato 2018).*
- So when establishing a "by object" restriction, regard must be held to "the content of the agreement, the objectives it seeks to attain, and the economic and legal context of which it forms part". *GlaxoSmithKline Services Unlimited v Commission*, joined cases C- 501/06 P, C-513/06 P, C-515/06 P and C-519/06 P 2009
- Essentially the deeming provision in The Malaysian Act precludes the use of economics in determining the circumstances under which 'object' must be demonstrated - unlike in the EU.
- So **form of the agreement dominates economics** in Malaysia – switching the burden of proof to the accused even when the conduct is patently economically beneficial. If **economics can be trashed** in the Act what further damage is caused in designing and interpreting guidelines and in decisions made by judges with negligible knowledge of economics - particularly where the digital economy is concerned

Is Asian Business Different?

- Witt and Redding (" Asian Business Systems: Institutional Comparison, Clusters, and Implications for Varieties of Capitalism and Business Systems Theory") argue that:

  "Asian business systems (except Japan) cannot be understood through categories identified in the West"

- Unfortunately, there is little informed understanding as to whether there are sufficient differences to justify a different Asian approach to competition law.

- Over the last 10-15 years, ethnic Chinese businesses in Southeast Asia have faced increased competition both from within their community and from without – especially from indigenous business. One of the important reasons for this is:

  "Insofar as Southeast Asian Chinese business communities are concerned, the most significant challenge to their material well-being is the potential dissipation of what Yoshihara (1988) termed 'ersatz capitalism' which refers to the rent-seeking behaviour of Southeast Asian Chinese capitalists through political-economic alliances with dominant ruling elites"
  Henry Wai-chung Yeing "Economic Globalization, Crisis and the Emergence of Chinese Business Communities in Southeast Asia" International Sociology Vol 15(2) June 2000, pp 266-287 at p. 277.

- Much more research is needed on whether competition law should adapt to any differences in Asian Business practices