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ANTITRUST IN TIMES OF FINANCIAL CRISIS

Anna Piszcz¹

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Abstract

The author attempts to answer the question of whether there is any role for antitrust policy and legislation to play in an era of financial crisis. The author analyses trends regarding concentration control, as well as enforcement of other antitrust rules in times of crisis. In this paper the author deals also with the question of what impact a chosen antitrust policy may have for future antitrust enforcement. Finally, the author attempts to forecast the consequences of a chosen antitrust policy.

Keywords: antitrust, crisis, competition, failing firm

Introduction

The current financial crisis began in 2007 in the USA and the country found itself in deeper trouble than at any time since the Great Depression of the 1930s. In the latter half of 2008 the crisis spread to EU, Japan, as well as other economies and has destabilised developed, emerging and developing countries. As regards Poland, in October 2008 - one of the worst months of trading in history of the Warsaw Stock Exchange - the Polish government still believed that our country was not experiencing a real crisis. However, the sudden weakening of the Polish zloty since the beginning of 2009 - to the lowest in five years - is one of proofs that Poland is indeed in a state of crisis. In Poland, like in many Eastern European countries and also in Iceland, New Zealand and Australia, it was beneficial for private households and enterprises to borrow - on a fairly large scale - in foreign currencies, particularly in the Swiss franc, at a lower rate of interest compared with local currency loans. Borrowers face a severe debt shock. Poland has also been hit by falling demand for exports. Notwithstanding, compared to what is happening internationally, Polish financial institutions, having relatively safe credit policy, are in a really good position despite connections with foreign banks and foreign markets.

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Role of antitrust rules

In the wake of the crisis, international institutions and governments around the world have taken a number of measures to ward off the impact of the global economic crisis, safeguard the stability of the financial markets and boost economic growth. On one hand, one can see a trend toward unilateral measures undertaken with national interests in mind, e.g. infusions of capital. Polish government, however, seems to be offering some unintelligible solutions which are hardly believed in. On the other hand, given the enhancing integration and interdependence of national economies and financial markets, governments are deliberating on the unification of unilateral tools, establishing a more coherent system as well as restructuring multilateral institutions and trading instruments.

Subsequently, interesting questions are brought up regarding the role of antitrust law - understood as the rules prohibiting agreements and practices that restrict free trading and competition, the rules prohibiting abuse of a dominant position, as well as the rules on control of concentrations (mergers and acquisitions) - in times of crisis. First, is there any role for antitrust policy and legislation to play in an era of financial crisis? If yes, what kind? Second, what impact may a chosen antitrust policy have for future antitrust enforcement?

Generally, there are two concepts of the role of antitrust rules: a traditional one according to which the role of antitrust law constitutes ensuring the freedom to compete, and one which states that the role of antitrust law constitutes making markets work well for consumers (Schmitz, 2002: 359). No matter which concept is chosen, the question arises as to whether this role - sometimes defined by the law itself (Miąsik, 2008: 34)² - is suspended, modified, limited or expanded in times of crisis. By this, I do not mean a legislative action aimed at reshaping the role of antitrust law but antitrust enforcement that evolves with time. Developed countries have antitrust legislative frameworks

² See Article 1 section 1 of the Polish Act of 16th February 2007 on competition and consumer protection (Journal of Laws No. 50, item 331, as amended): "(...) *development and protection of competition as well as (...) protection of interests of undertakings and consumers, undertaken in the public interest*".

appropriate for times of growth as well as a recession. The open question is how to enforce these solid foundations.

Concentration control

Conducting antitrust proceedings is a time-consuming process whereas in circumstances of widespread crisis, there are groups of interest like politicians or businesses that look to quick fixes. However, this does not result in the pressure to suspend antitrust enforcement in its entirety but one can observe the demand for selective antitrust enforcement. A desire for some selectivity in the application of antitrust rules is expressed, in particular for not applying antitrust rules that does not allow permitting anticompetitive mergers. Saving businesses from failure should preponderate over antitrust principles. According to this logic, tightened merger review should be shunted aside.

As regards mergers, two contradicting trends can be observed around the world in times of crisis. On one hand, in some markets one can observe an increasing merger wave (Stolz, 2007: 94). On the other hand, there are markets where mergers and acquisitions seem to be typical of times of prosperity whereas in times of crisis enterprises are more oriented towards protecting their hitherto positions in the market. Polish markets can be used as examples of this second tendency. During the first two months of 2009, Polish national competition authority – the President of the Office of Competition and Consumer Protection (OCCP) received only 9 M&A notifications. This is only one third of the number of notifications received in January and February 2008.

Regardless of which of these trends actually wins, according to the “theory” of selective enforcement, in the course of merger assessment proceedings the highest priority should be afforded to restructurings that are necessary when countries are recovering from crises. To achieve this, the competition authorities should turn a blind eye to the risk of acquiring a market power by the merging parties.

The possibility of such a change of the role of antitrust enforcement mainly depends on flexibility of legislative regime. However, almost all jurisdictions can recognise a so-called failing firm defence (failing firm doctrine), i.e. that the failing firm is going out of business and the only

way to save it is for the buyer to take it on. The practical application of the failing firm defence may vary from authority to authority. The European Commission and the competition authorities of the Member States (e.g. the United Kingdom, Poland) used to apply this doctrine very narrowly. The European Commission has recognised the possibility of the failing firm defence indicating three cumulative criteria which are relevant for the application of this defence³: (1) the failing firm would in the near future be forced out of the market because of financial difficulties if not taken over by another undertaking; (2) there is no less anti-competitive alternative purchase than the notified merger; and (3) in the absence of a merger the assets of the failing firm would inevitably exit the market.

As regards Poland, the Act of 16th February 2007 on Competition and Consumer Protection states that concentration control is not applicable at all when the concentration arises as an effect of insolvency proceedings (excluding the cases where the firm is to be taken over by a competitor or a participant of the capital group to which the competitors of the to-be-taken firm belong)⁴. In the case when the firm has not yet been subjected to insolvency proceedings, the failing firm defence (*sui generis*) may be based upon Article 20 section 2 of the Act which provides that the President of the OCCP issues a consent for the implementation of the concentration as a result of which competition in the market will be significantly impeded, in particular by the creation or strengthening of a dominant position, in any case that the desistance from banning concentration is justifiable, and in particular:

- 1) the concentration is expected to contribute to economic development or technical progress;
- 2) it may exert a positive impact on the national economy.

These provisions are drafted in such a general and imprecise language that they leave an interpreter with wide margins of discretion and, thus, may be understood and applied in a substantially different way in times of crisis and in normal times. However, in Poland, the financial crisis has not caused any so-called “shotgun marriages” in the domestic banking

³ Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, Official Journal C 31, 05.02.2004, p. 5-18. The Commission’s view is consistent with the ECJ judgment in *Kali und Salz* case (joined cases C-68/94 and C-30/95), [1998] ECR I-1375.

⁴ Article 14 item 4.

sector so far. Moreover, to date, the President of the OCCP has been silent of its views of the role of antitrust law and policy in an era of crisis⁵.

The United Kingdom's approach to the failing firm defence is described succinctly in the guidelines of the Competition Commission and in the guidelines of the Office of Fair Trading⁶ (Parr, 2005: 384). In 2008 both authorities launched a joint review of their guidelines for the assessment and review of mergers in order to produce a single set of guidelines. Notwithstanding, on 18th December 2008 the OFT published a restatement of its position on the failing firm defence in merger analysis. According to the abovementioned restatement, in order to apply the failing firm defence, two conditions must be satisfied: "inevitable exit" condition and the absence of an alternative purchaser. The OFT also made clear that, in line with recent practice, it would offer informal, confidential guidance to parties to the merger relying on the failing firm defence.

In Canada the failing firm defence is incorporated in the Competition Act and the Merger Enforcement Guidelines of the Competition Bureau. Besides, Canadian competition law provides for an efficiency defence, which allows anticompetitive mergers to be approved if they are likely to generate gains in efficiency that will be greater than, and will offset, the effects of any prevention or lessening of competition (Addy, 2008: 9).

However, the unique possibilities of selective antitrust enforcement are offered by the U.S. antitrust regime which in comparison to other national regimes appears extremely flexible. Although American antitrust rules remain almost unchanged for over a hundred years, antitrust enforcement reflects changes of existing economic circumstances and social needs as well as of economic theories and legal concepts. In the USA, having regard to the current economic environment, three grounds should be mentioned that determine the possibility of clearing anticompetitive mergers: (1) the failing firm defence under the 1992

⁵ The only context in which the President of the OCCP referred to the financial crisis was state aid. It is interesting that the beginning of 2009 brought one prohibition of the concentration (fourth from 2004) and one conditional approval of the concentration (ninth from 2004). Perhaps the President of the OCCP has been too permissive in reviewing mergers.

⁶ Hereinafter referred to as the OFT.

Horizontal Merger Guidelines⁷, (2) the General Dynamics defence and (3) the flailing firm defence. The flailing firm defence focuses on the following aspects: the firm will be unable to meet its obligations in the near future, the flailing firm has no realistic prospect for a successful reorganisation, there is no identifiable purchaser that would not pose antitrust concerns, and the assets would likely exit the market absent the transaction. The General Dynamics defence relies on the U.S. Supreme Court's decision⁸ where the Court concluded that, even provided that a company was not going to exit the market, if the company lacked resources to be able to engage in new competition in the future, acquisition of that company would not be unlawful. On the contrary, the flailing firm defence - a variant of the General Dynamics defence - may be applied when the firm would likely have some competitive influence going forward⁹.

It seems that no matter what views the competition authority might hold on the two last of the aforementioned defences, the crisis might cause it to be more receptive to the needs of businesses. There are numerous examples of this kind of policy applied because of the urgency of the situation. I wish to express amazement at the extent to which the USA facilitated major mergers in the financial sector that would raise some antitrust concerns if they were reviewed in normal times. For example, Wells Fargo's application to acquire Wachovia Corporation was approved by the competent authorities "in light of the unusual and exigent circumstances affecting the financial markets, the weakened financial condition of Wachovia". Also Bank of America that acquired two troubled giants: Countrywide Financial and Merrill Lynch took advantage of the economic instability, benefiting from the lax decisions by the authorities. Next, JP Morgan Chase acquired both Bear Stearns and Washington Mutual as those financial institutions crumbled under a financial and market meltdown. This series of so-called "shotgun marriages" (Rich, 2008: 1) was arranged to stave off bank failures¹⁰.

⁷ The Guidelines incorporate considerations of the U.S. Supreme Court - decision in *Citizen Publishing Co. v. United States*, 394 U.S. 131, 136-38 (1969).

⁸ *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974).

⁹ *United States v. UPM-Kymmene Oyj*, 2003 WL 21781902, 2003-2 Trade Cas. (CCH) 74,101 (N.D. Ill. 2003).

¹⁰ The review process for bank mergers differs from that for other transactions. Banking industry-specific statutes govern most bank mergers reviews. For any particular transaction, one of four banking agencies (the Federal Reserve Board, the Federal

Proper merger analysis of a transaction that raises competition issues takes much time whereas restructurings are usually urgently needed to maintain the economic stability. Speed of response does not necessarily go hand in hand with fulfilling usual roles of antitrust law. Therefore, the competition authorities are more open to play the emergency role to rescue economies if they are equipped with some “corrective” tools. Such a “safety valve” exists under section 97 of the Canadian Competition Act which authorises the Competition Bureau to challenge a transaction up to three years following closing. The U.S. competition authorities possess a tool such as the “pocket decree” (or “blank check”) that permits a transaction to close immediately, but also permits the authority to require a divestiture at a later date if the authority concludes that a remedy is necessary. These tools provide authority with some comfort but the other side of the coin is the uncertainty of decisions by the authority.

Without a doubt the competition authorities need to engage closely with government attempting to save the financial system. However, as proved by the United Kingdom’s experience with an acquisition by Lloyds TSB of HBOS (where the government - exercising statutory powers granted to the Secretary of State under section 42 of the Enterprise Act of 2002 - withdrew jurisdiction from the antitrust authorities to review the merger despite antitrust concerns), political pressures to act quickly may not allow any meaningful role for antitrust review. The public interest may be prioritised, in particular when the authorities consider action in national sectors. The United Kingdom’s Parliament altered the regulatory framework for financial sector mergers to enable the public interest concerns to outweigh the competition issues.

Enforcement of other antitrust rules

A second point brought out by the “theory” of selective enforcement is that the enforcement of some antitrust rules should be more robust in order to do properly its job of protecting consumers from abuses in times

Deposit Insurance Corporation, the Office of Thrift Supervision or the Office of the Comptroller of the Currency) shares jurisdiction with the Department of Justice’s Antitrust Division.

of crisis. It is possible that the competition authorities - bowing to political pressure - initiate investigations that would not be commenced in normal times. We find an example of such proceedings during the U.S. gas price crisis of 2004 when the Federal Trade Commission opened an investigation of the decision by Shell Oil Products US to close its petroleum refinery in Bakersfield (California). Finally, the Commission closed its twelve-month investigation but from the beginning it was quiet clear that an independent decision by a non-monopolist to close a plant is not something that may have antitrust implications.

A pressure for stronger cartel enforcement may also arise. During periods of economic crisis, the temptations for businesses to collude and establish new cartels to “share the pain” may increase. This increase may be accompanied by a decrease in the volume of leniency applications. Thus, there is nothing surprising in the fact that the competition authorities may enhance their efforts to detect illegal cartel behaviours undertaken to deal with economic pressures.

However, it may be difficult for the competition authorities to escalate a scale of fines and, therefore, in some countries there may emerge a demand for new methods of deterrence, such as jail sentences (Cseres, 2006) or sanctions for individuals (Jones, 2007: 1211). Notwithstanding, the contradicting trend may be found in the European Commission’s antitrust enforcement as one can observe the record fines of over Euro 1.3 billion relating to the car glass cartel imposed in November 2008. It can be seen that the Commission has little intention of weakening its enforcement stance in the face of the current crisis.

On the other hand, the question arises as to whether the so-called crisis cartels could be allowed in times of crisis. The European Commission responded to the formation of “crisis cartels” in the 1980s (Wesseling, 2000: 38). The Commission exempted under Article 81(3) of the EC Treaty an agreement to make specific production cutbacks to deal with the overcapacity that the industry suffered from (Commission Decision of 4th July 1984, 1984 OJ L207/18), as well as a market-sharing agreement that enabled the parties to eliminate underutilised capacity, improve unit costs and eliminate losses (Commission Decision of 19th July 1984, 1984 OJ L212/1). Yet, the Commission - under its Guidelines on the Application of Article 81(3) of the EC Treaty - has not made any

statements that would indicate its position in the current economic downturn. Thus, the exemption criteria must be construed narrowly, as usually.

Similarly, the availability of exemption for crisis cartels under Polish law is in principle limited. The Polish equivalent of Article 81(3) of the EC Treaty requires an agreement to: (1) contribute to improvement of the production, distribution of goods or to technical or economic progress; (2) allow the buyer or user a fair share of benefits resulting thereof; (3) not to impose upon the undertakings concerned impediments which are not indispensable to the attainment of these objectives; and (4) not to afford these undertakings the possibility to eliminate competition in the relevant market in respect of a substantial part of the goods in question.

Consequences of a chosen antitrust policy

Global economic crisis needs a global response. The United Nations Conference on Trade and Development (UNCTAD) prepared a report titled "The Global Economic Crisis: System Failures and Multilateral Remedies". The issue of competition is shortly highlighted in Chapter V where it is stated as follows: *"(...) countries that want to share the potential benefits of the trade and foreign direct investment have to understand that the creation of level playing fields for the competition of the companies is a desirable target but that competition of nations is useless and dangerous concept. (...) To avoid the fight for market shares through manipulation of the exchange rate, wage rates, taxes or subsidies and to prevent financial markets from driving the competitive positions of nations into the wrong direction, a new code of conduct is needed regarding the overall competitiveness of nations"*.

It seems that domestic remedies shall not be abandoned in favour of an internationally coordinated intervention, and thus, national antitrust issues shall not be relegated to a second tier policy imperative. However, a difficult challenge for national competition authorities around the world is to internationalise their policies and approaches as the global trade negotiations known as the Doha Round broke up without an agreement (Evenett, 2006: 454). Countries cooperate on a bilateral and multilateral basis in area of competition, mostly on a voluntary, nonbinding basis, which results in *de facto* harmonisation through co-

operation. A possible benefit of the current economic crisis may be a greater internationalisation across the global antitrust enforcement community. The enforcement posture of one jurisdiction may result in adoption of the same stance in other jurisdictions, e.g. increased enforcement in one jurisdiction may lead to increased enforcement in other countries.

What impact may a chosen antitrust policy have for future antitrust enforcement? It depends *inter alia* on the remedies used. Actions taken in a crisis atmosphere may produce consequences and generate controversy for years to come (Winerman, 2008: 2). Those who present the approach of getting through the crisis and dealing with negative consequences later seem to forget that facilitating mergers may increase concentration and lead directly to higher prices. Increased prices are almost always accompanied by reduced output and in turn more unemployment. This may lead the competition authorities to investigate more abuse of dominance cases in the future. However, it is safe to say that one cannot expect a financial crisis to give anyone a free pass where antitrust enforcement is concerned.

Concluding thoughts

The history of the current financial crisis has yet to show whether antitrust rules and antitrust enforcement shall be a hindrance or an aid to the effort to solve the crisis. In my opinion, antitrust enforcement may be part of the solution to the crisis, rather than the problem, although the rush to solve the crisis seems to be ignoring the relevance of antitrust rules. It is hard to say whether antitrust policy will remain relevant to the crisis, or it will have little meaningful impact on the crisis outcome. The debate continues and will likely continue during the next few quarters.

I would suggest that competition laws need to be implemented at least as strictly during a time of economic crisis as they are in normal times. A strong and effective competition law designed for the evolving market conditions allows for flexible application of antitrust rules without weakening enforcement stance or radical shifts in the key enforcement priorities. It seems that it is possible to integrate the usual functions of antitrust rules with their emergency role, to some extent. Moreover,

antitrust crisis enforcement may also play the role of a factor accelerating internationalisation of antitrust policy.

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