# COMMENT & ANALYSIS

## INTERAC, ESSENTIAL FACILITIES AND ACCESS TO ELECTRONIC FUNDS NETWORKS: A COMMENT ON MATHEWSON AND QUIGLEY

By: Brian Rivard,* Competition Bureau and
Roger Ware,** Queen's University

In the Summer 1997 issue of the *Record*, Frank Mathewson and Neil Quigley ("MQ") published a refreshingly critical review of the Consent Order approved by the Competition Tribunal in the *Interac* case.[1] Their article casts stones in many directions, but focuses its criticism essentially on two points. First, that Interac is a bad candidate for an essential facility, and that an abuse of dominance case resting heavily on such a designation was not well founded. Second, the true identity of the essential facility, and the true source of restricted competition in financial services are the rules and governing framework of the Canadian Payments Association (the "CPA").

We do not disagree that the rules of the CPA have restricted competition in the broad market for financial services (particularly in the market for demand deposits), and that a relaxation of those rules is desirable. However, it is quite erroneous to argue, as MQ have, that a change in the framework and regulations of the CPA to allow broader CPA access to financial service providers would have been *sufficient* to restore competition in the markets identified by the Director in the Interac case.[2] MQ's position that the Interac case should have been *about* the CPA and not about the Interac Network is ill-founded. In this article we explain why the Interac Consent Order was necessary to restore competition in the market for Shared Electronic Financial Services ("SEFS").

In particular we argue that: (i) allowing broader access to the CPA alone, without intervention directly focused on Interac, would not have provided these institutions access to the Interac network or to an alternative network of any significant size; and (ii) even if access to Interac was broadened to include suppliers of financial services, insurance companies and other agencies, this access alone would not have been sufficient to restore competition in the market for SEFS. The Director's case dealt with a variety of anti-competitive concerns, many of which were independent of the access issues identified by MQ.[3] For these reasons, the Interac Consent Order was necessary to restore competition in the market.

**Opening Up the CPA without any Changes to Interac: a Counter-Factual Experiment**

In their paper, MQ propose that the real competition problem in the Canadian payments system is the regulatory framework of the CPA. They argue that "the CPA Act and the regulations developed by the CPA currently prohibit insurance companies and fund managers from any direct participation in the payment system"[4] and that "(i)n the absence of this regulatory barrier, ... competition will provide for the efficient operation of the Canadian payment system."[5] MQ's position is that changes to the CPA's regulatory framework alone would have been sufficient to restore competition in the market identified by the Director in the Interac Consent Order: namely the market for SEFS. In other words, providing non-financial institutions ("non-FIs") access to the clearing and settlement services of the CPA would have removed all impediments to these institutions supplying SEFS to their customers.

While major changes to the regulatory framework of the CPA could allow non-FIs to participate directly in the Canadian payments system, such changes alone would not have enabled non-FIs to offer shared financial services on a network of any significant size. To establish the inadequacy of the MQ proposal, we consider the following counter-factual experiment. Suppose that MQ's advice had been followed, and any financially viable institution was eligible for membership to the CPA, to undertake clearing and settlement activities. Suppose also that there had not been, and would not be, any intervention by the Director into the operation of the Interac Network. Under this scenario, we ask whether non-FIs would have been: (i) permitted to participate in the Interac Network to offer shared financial services; or (ii) able to establish or join a similar EFT network which could have duplicated the level of services offered by the Interac Network in any economically viable manner? We address both of these questions below.

*(i) Participation in Interac by Non-FIs*

Under the old Interac rules and governing by-laws, non-FIs (and smaller FIs for that matter) would not likely have been allowed or able to participate in the Interac Network. It is true that *conditional* on obtaining Interac membership, liberalized CPA access would render some restrictions redundant, such as the restriction that chartered members and sponsored members of Interac must be members of the CPA. Nevertheless, there is abundant evidence that the chartered members of Interac designed the governance structure to exclude new members. It would have been easy and relatively costless to tighten the Interac by-laws to maintain this exclusion in response to any relaxation of CPA membership.

Indeed, Interac made such changes to its rules and by-laws in at least two instances. First, when AMEX (a CPA member) first considered joining Interac in 1988, the entry fee was a flat fee of $100,000. After AMEX expressed its interest in joining Interac, the Chartered members of Interac effectively increased the entrance fee of Amex to $11 million by introducing a per card entrance fee of $7.50.[6] Second, in 1988 Royal Trust and the General Motors Acceptance Company ("GMAC") entered into an arrangement which allowed GM employees to invest in a GMAC demand note simply by using an Interac ABM. The arrangement,

which involved a Type I sweep account, led to an amendment in the Interac by-laws which banned all sweep accounts between members and non-members.[7] It seems clear from both the AMEX and GMAC/Royal Trust examples that a freeing up of the CPA rules would have been followed by a corresponding tightening of the Interac rules and by-laws by the chartered members. Direct participation in the CPA would not necessarily have implied access to the Interac Network.

Furthermore, if they had wanted to preclude institutions from participating in Interac, the chartered members of Interac could have responded to any changes in the regulatory framework of the CPA by establishing an independent clearing and settlement body within the Interac Network.[8] A U.S. expert presented evidence to the Interac hearings that the costs of Interac establishing its own clearing and settlement arrangements were quite small.[9] Although this evidence was cited by the Tribunal to indicate that the CPA might be acting as a spurious barrier to entry to Interac,[10] in fact it also demonstrates that under a liberalized CPA a self-clearing system could itself have acted as a barrier to entry.

In sum, without the Interac Consent Order the chartered members of Interac would have likely established restrictive eligibility criteria to preclude unwanted participants from accessing the Interac Network. The only recourse of these institutions would have been to attempt to join together with other excluded institutions to start their own electronic funds network, requiring a large scale investment in terminals.[11]

(ii) *Duplication of the Shared Services of Interac*

MQ's position is that "the ability to participate directly in the payments system, not the ability to access Interac, represents the essential facility."[12] According to this view, absent the regulatory barriers of the CPA, non-FIs could establish new Electronic Funds Transfer ("EFT") networks to compete against the Interac Network. However, if non-FIs were precluded from participating in the Interac Network, would their direct participation in the CPA have enabled them to provide for their customers the type of shared services offered by Interac by establishing or joining another EFT Network? In our view, providing non-FIs with CPA membership would not have aided the establishment of an EFT network competing with Interac.[13]

Interac was a joint venture which connected the proprietary ABM networks of the founding chartered members.[14] This joint venture provided the demand deposit customers of these institutions with the convenience of extensive ABM access to their demand deposits. At the time of its inception, the chartered members of Interac collectively accounted for more than 95% of the ABMs deployed in Canada and 90% of Canadian demand deposits. For a new EFT network to establish itself in Canada as a competitor to Interac, it would have had to duplicate the terminal coverage (ABM and Point of Sale ("POS")) of Interac. It would also have had to attract a similar deposit base to support the extensive ABM coverage. Given the 9 largest demand deposit taking institutions were the chartered members of Interac (and the Interac by-laws created huge disincentives for leaving Interac) it would have been virtually impossible to duplicate

this base.[15] This is the facility (the terminal coverage and demand deposit base) that is economically infeasible to duplicate. As a result, it is unlikely that direct participation in the CPA, absent the Consent Order, would have been sufficient for non-FI financial service providers to offer SEFS to their customers through an alternative network to Interac.

**Essential Facilities and Access to Network Joint Ventures**

MQ have built up something of a straw case to shoot down in their quest for deregulation of the payments system. They set up their own definition of an essential facility, then claim that the Director's case depended heavily on the designation of Interac as an essential facility, as defined by MQ. In fact neither the Director's Application nor the Decision of the Competition Tribunal, nor any other of the Director's document in the Interac case of which we are aware uses the term essential facility with reference to Interac. Instead, the case presented by the Director rests squarely within the framework of U.S. jurisprudence covering access to network joint ventures, which we review briefly below.

The first landmark U.S. case was the PULSE arbitration in 1982. Texas had two competing EFT networks, PULSE and MPACT. First Texas Savings and Loan Association, a large thrift institution, was already an MPACT member and was prevented from joining PULSE by their exclusive membership rule. A U.S. Department of Justice ("DOJ") brokered arbitration led to First Texas being admitted to PULSE.[16]

Similar issues were raised in the MountainWest case in 1994. Dean Witter, then a subsidiary of Sears, failed in its bid to issue a low priced Visa card. Dean Witter's Discover card was already a significant competitor to Visa. Even though Visa had an open access policy, it invoked a rule that issuers of rival cards could not be members of Visa. The jury found for Dean Witter, but the Tenth Circuit reversed the finding, holding that, as a matter of law, Visa could not exercise market power because it is made up of thousands of independent competitors.

A central issue in these cases is the trade-off between *intersystem competition* (competition between competing networks), and *intrasystem competition* (competition between members of the same network). When a financial institution joins a dominant network, either from an independent position or previously as a member of a smaller network, intersystem competition will be reduced and intrasystem competition (to the extent the network permits such competition) increased. The net effects of such a change will depend on a careful study of the particular case, but could increase or decrease overall economic efficiency.

On the one hand, society benefits from the inclusiveness of a network joint venture since it is characterized by positive network externalities. On the other hand, denying access to a network joint venture may be efficient if: (i) the excluded firms represent a constraining competitive influence to the network and their exclusion promotes lower prices, more product variety or innovative behaviour; (ii) it is necessary for the

network to exclude certain firms so as to ensure the security, integrity and overall quality of the network service; and (iii) the supercompetitive profits generated by excluding access to these firms is necessary in order to induce firms to undertake the risky investment required to develop these networks.

An important issue for antitrust authorities in these cases is under what, if any, circumstances intervention should occur to compel a private joint venture to include or not include certain competitors. Some antitrust scholars believe that a joint venture should not be subject to intervention unless there is a clear abuse of a dominant position. Others are more disposed to forcing access if it can be shown that the joint venture: (i) harms competition and (ii) there are no demonstrated efficiency advantages to the access restriction.[17]

In terms of the Interac case, the Director's investigation concluded that there was a clear abuse of a dominant position. In the Notice of Application, the Director made the following allegations. First, the respondents collectively had market power in the provision of shared electronic network services (i.e., the input required to enable network participants, including potential network participants, to provide the final product, SEFS). This market power was derived from their collective dominance in ATM deployment and the supply of demand deposits, coupled with the usual demand externalities associated with an EFT network.

Second, the respondents jointly engaged in anti-competitive practices. First, the respondents, through the enactment of exclusionary by-laws, imposed certain restrictive policies, conditions and requirements that limited the eligibility of candidates for membership into the Interac network (prevented intersystem competition). Second, the respondents enacted by-laws and operating regulations which effectively curtailed competition between themselves in both the input market and the final product market (prevented intrasystem competition). These anti-competitive practices had the effect of substantially lessening competition in the final product market, the market defined as SEFS.

Much of the Director's case focused on those practices which curtailed competition between the Interac members in both the input market and the final product market (prevented intrasystem competition). These practices included: (i) the restrictions on membership and membership status which ensured that the nine chartered members of Interac maintained effective control over the governance of Interac and the Interac shared services; (ii) the collective setting of the interchange fee along with the no surcharge rule which promoted monopoly pricing at the terminal level; and (iii) the restrictions allowing only existing shared services or shared services approved by the chartered members to be offered.[18] The Consent Order focused on removing these restrictions and promoting intrasystem competition.

We would argue that even if broader access had been granted to the CPA and the Interac network to include other financial service companies, this access in itself would not have been sufficient to restore competition in the market for SEFS. Without the Director's Application the restraints on intrasystem competition would likely have remained in place.

We return now to the issue raised by MQ as to whether Interac is an essential facility. Earlier we pointed out that the Director's case against Interac was not based on an essential facilities argument, nor did it require one. Rather, Interac was an abuse of dominance case involving a network joint venture, whose remedial focus was to restore competition within the Interac Network for the provision of SEFS largely by removing impediments to intrasystem competition. These included the chartered members' restrictive by-laws and policies regarding network access and participation.

An EFT network involves two economically distinct but complementary activities: issuing and acquiring. The issuer supplies the cards that are used at ATM and POS terminals sponsored by other members of the network. The acquirer is the sponsor of the terminal, and undertakes to pay out cash or carry out another transaction when instructed by the cardholder. The essence of a shared EFT network is that the issuer and acquirer can be different members of the network.

The barrier to entry, or essential input that is economically infeasible to duplicate, is different for potential issuers and potential acquirers. For issuers it is the installed network of terminals, plus some access to the settlement system for transactions. For potential new acquirers, such as retailers, the essential input is access to the installed base of Interac cardholders together, again, with access to a settlement system. Each of these would be difficult or prohibitively expensive to duplicate by new entrants in order to create a competing network. Thus, MQ's statement that

> (w)e have substantial doubts that Interac is an essential facility because the messaging system could be reproduced at relatively modest cost[19]

misses the point. The costs of constructing a message system are small, but a message system is of little use if it does not connect to the essential elements of a viable EFT network: terminals and cards.

**Was Interac the Right Target for the Director?**

The main thrust of MQ's criticism is that Interac was the wrong target for a competition policy intervention, and that the correct target is the CPA. We have argued that liberalizing access to the CPA alone would not have been *sufficient* to restore competition in the market for SEFS. Furthermore, it was clear to all parties during the Interac investigation and Hearings on the Consent Order, that the Tribunal does not have jurisdiction to grant institutions with membership in the CPA; this remedial order was not available to the Director.[20] In attempting to restore competition in electronic financial services, the Director had recourse *only* to the industry itself, in particular Interac, and was unable to petition the Competition Tribunal to invoke regulatory changes to the CPA Act. Given the existing CPA framework, the rules of Interac prevented competition in electronic funds services, and the changes implemented in the Consent Order will benefit competition and the consumer.

**Overall Competitive Impact of the Interac Consent Order**

The Interac Consent Order was implemented in November 1996. In contrast to the pessimism expressed by Mathewson and Quigley we see encouraging evidence that the Order has facilitated an increase in competition in several areas. We briefly review this evidence below.

*Access*

Since the Consent Order was implemented in November 1996, membership has increased from 27 to 50 members, including more than five non-FIs. Under the terms of the Consent Order, two of the latter new members have board representation.

*Indirect Issuance under Sweep Arrangements*

A substantial part of the Interac hearings in April 1996 were taken up with a debate about whether liberalized arrangements on sweep accounts[21] would facilitate access to the Interac network by would-be card issuers, such as life insurance companies and mutual fund companies. The Director expressed the view that "indirect issuance" arrangements would emerge, employing sweep accounts with an FI CPA member. Unfortunately, little progress has occurred so far in this area. A major stumbling block is that the CPA has not yet facilitated Type II sweep accounts, also known as payable through accounts.[22] With these accounts, an account holder at a non-FI, such as a life insurance company, would be able to have a card issued against their liquid life insurance funds; only the life insurance company need hold an account with a CPA member FI, not each individual cardholder.

With respect to payable-through arrangements, the CPA has stated:

> The desire of corporate entities to provide their clients with convenient access to funds via payable-through arrangements is essentially equivalent to asking for the main benefit of being a CPA member, namely, access to the ACSS without having to meet the underlying system-wide regulatory requirements, obligations and responsibilities associated with being a CPA member. To preserve the safety, soundness and efficiency of any expanded Canadian payments system, it is critically important that a public or system wide framework be established, setting out criteria for access to the payments system whether it be access in the form of CPA membership or access through the use of payable-through arrangements. The framework should contain elements having the objectives of: (i) ensuring continued consumer confidence in the payments system (by the effective management and disclosure of the risks to consumers); and (ii) fostering a competitive environment for all industry participants.[23]

*Entry into Acquiring and Installation of New Terminals*

Prior to the Interac Consent Order, the Interac by-laws required that an acquirer of Interac transactions must also be a card issuer. Card issuers, of course, had to be CPA members. The consent order broke this link, and paved the way for entry by independent acquirers. Contrary to the claim by MQ that there

are "economies of scope between acquiring and issuing"[24] - the reason that current Interac members engage in both activities is because they were required to do so, and the industry has not yet settled down to a new post-Consent Order equilibrium. In support of the fact that acquiring will be a profitable activity for non-issuers we can appeal to examples of such entry taking place. As reported recently in the *Globe and Mail*[25] one independent deployer of Interac ATMs plans to install up to 1,000 new terminals.

The profitability of entering the acquiring business is fairly transparent. Each Interac SCD transaction generates an *interchange fee* of 75 cents paid by the issuer to the acquirer.[26] In addition to the 75 cents, ATM deployers may now levy a surcharge at the terminal of their own choosing, and the entrant reported above is levying approximately $1.00 per transaction. With the cost of an ATM as low as $25,000, the opportunities for profit are clear.

We remain puzzled as to why both MQ and the Tribunal did not perceive these profitable opportunities for new ATM deployment. The confusion may have arisen because the number of terminals per capita is relatively high in Canada. But a high average density does not imply an efficient pattern of deployment, especially when interchange fees and the former ban on surcharges created an artificial incentive to expand the number of ATMs (even pre-Consent Order). The introduction of surcharging should lead to a more efficient deployment pattern, which in long run equilibrium could imply greater or fewer total number of ATMs.[28]

In addition to at least one new entrant in Shared Cash Dispensing, two new acquirers have entered the POS side of Interac and are offering retailers improved IDP terminals. Another new direct connector is offering retailers or other institutions connection to Interac.

*New Services*

The changes in the governance structure of Interac effected in the Consent Order have created an environment much more conducive to the introduction of new services. For example, Interac is reportedly considering the introduction of a shared bill presentment service as well as improving ABM functionality to permit shared deposit acceptance, balance inquiry and balance transfer services.

**Conclusion**

We do not accept MQ's argument that the ability to directly participate in the CPA alone would have been sufficient to restore competition in the market for SEFS. In our view, access to the CPA would not have guaranteed fund managers, insurance companies and other agencies the ability to offer SEFS through Interac or any other Network of significant size. Without the Director's Application to the Competition Tribunal and the resulting Consent Order, competition would not have been adequately restored in this market.

**References**

Carlton, D. W. and A. S. Frankel, 1995a "The Antitrust Economics of Credit Card Networks" *Antitrust Law Journal* 63: 643-668.

Carlton, D. W. and A. S. Frankel, 1995b "The Antitrust Economics of Credit Card Networks: Reply to Evans and Schmalensee Comment" *Antitrust Law Journal* 63: 903-916.

Evans, D. S. and R. Schmalensee, 1995 "Economic Aspects of Payment Card Systems and Antitrust Policy Toward Joint Ventures" *Antitrust Law Journal* 63: 861-902.

McAndrews, J.J. and R. Rob, 1996 "Shared Ownership and Pricing in a Network Switch" *International Journal of Industrial Organization* 14: 727-745.

**Notes**

* The views expressed by Brian Rivard in this article reflect his opinions only and do not indicate the position of the Director of Investigation and Research or that of any government agency.

** Roger Ware acted as an economic expert for the Director during the Interac investigation and the hearings held by the Competition Tribunal in April 1996.

1 G.F. Mathewson and N.C. Quigley, "What's Essential, What's Prudential, What Can Competition Provide?" (1997) 18:2 Can. Comp. Rec. 11; *Director of Investigation and Research* v. *Bank of Montreal et al.* (1996), No. CT 95/2 (Comp. Trib.) (hereinafter "*Interac*").

2 MQ define access to the payment system as the ability to directly enter payment items to the CPA for clearing and settlement. Mathewson and Quigley, *ibid.* at 15.

3 The Interac Consent Order covered a wide range of issues concerned with access to, pricing and governance of the Interac Network. The hearings held in front of the Competition Tribunal in March and April 1996 covered only two issues, both related to access: namely, (i) the viability of indirect card issuer arrangements, such as sweep accounts and payable-through accounts, for institutions ineligible for CPA membership; and (ii) the viability of entry to the network by entities that would participate only as acquirers and not as issuers. MQ's comments pertain largely to the issues covered in the hearings, and thus do not reflect on many, perhaps, most aspects of the Consent Order.

4 Mathewson and Quigley, *supra*, note 1 at 12.

5 *Ibid.*

6 In 1988, American Express Travel Related Services Company, Inc. applied to federal regulatory authorities to obtain a banking license for the AMEX Bank of Canada ("AMEX"). This license provided AMEX with the ability to directly participate in the CPA. In fact, the primary reason for AMEX seeking this license was to enable it to satisfy the CPA membership qualification that was (before the Consent Order) a prerequisite for membership in Interac. At about the same time, the charter members undertook a review of Interac's membership criteria and access fees, and for 9 months suspended the admission of new members. In 1989 the By-laws of Interac were amended. These amendments substantially increased the cost of new sponsored membership by imposing a service access fee of $7.50 per card eligible to access the Shared Cash Dispensing service. Prior to these By-law changes, AMEX could have joined Interac as a sponsored member for a flat access fee of $100,000. The charter members' adoption of a service access fee of $7.50 per card had the effect for AMEX of increasing the total fees for SCD service access for its entire charge card base to more than $11,000,000. AMEX initially thought that this access cost was "excessive" and so sought other means to provide its cardholders with SEFS in Canada. In 1992, after a few failed attempts of finding substitute means of Canadian entry, AMEX joined Interac as a sponsored member. AMEX issued only a limited number of cards, in response to the high per card cost of membership. While this example probably best illustrates Interac's ability to extract monopoly rents from potential network participants, it also provides an indication of how easily the chartered members could have changed the rules or by-laws of Interac to exclude unwanted applicants.

[7] Cardholders were required to maintain a demand deposit account with Royal Trust. They could then, using an ABM connected to Interac, transfer funds from their Royal Trust account, to an account named "other" which was a dummy account set up by Royal Trust for the sole purpose of sweeping the money from this account into a GMAC account. Similarly, the consumer could access these invested funds through ABMs connected to Interac by simply withdrawing from a specific "other" account. In 1989, in response to this arrangement and other similar arrangements which were beginning to be established with non-FIs, the chartered members of Interac introduced a by-law that prohibited the use of what was termed "pass-through, zero balance or sweep accounts" in association with the Interac Network. This successfully terminated the GMAC/Royal Trust arrangement as well as other similar arrangements which were being contemplated.

[8] The Director acknowledged and the Tribunal appeared to accept that establishing an independent clearing and settlement service outside of the CPA was possible. The Director stated that "(a)nother mechanism could be used for clearing and settlement, provided that it was one that was acceptable to and used by each of the other network members." (Written argument of the Director at paras 139, 143).

[9] In his testimony, L. Carmody stated that "you could actually run a clearing system with Interac manually with ledger paper and a pencil. You are only settling between nine organizations. You are net settling every day, so the amounts of money aren't that great." (Transcript at 5:857 (16 April 1996)). To establish an independent clearing and settling body, Interac would have to replicate the settlement function performed by the Bank of Canada in the CPA. One institution could hold settlement accounts for each of the clearing members of Interac. These accounts would consist of liquid assets such as cash or securities. Since the banks are required to be members of the CPA and all direct clearers of the CPA are required to hold settlement accounts at the Bank of Canada, clearers of the new Interac system would incur an additional cost in terms of the opportunity cost of the liquid funds held at the new settlement institution.

[10] *Interac*, *supra*, note 1.

[11] Or possibly to rent space on Interac members' terminals; which would probably not have been forthcoming.

[12] Mathewson and Quigley, *supra*, note 1 at 12.

[13] In support we note three examples of failed attempted entry. In 1991 as a result of the exclusionary changes that the Charter Members made to Interac's membership fees and EFT/POS participation criteria, a number of smaller financial institutions (Alberta Treasury Branches, AMEX, Central Guaranty Trust, Hong Kong Bank, Montreal Trust, National Trust and Royal Trust) who were all eligible for CPA membership, sought to establish a new shared EFT network service to be called Sunrise. This network was to offer point of sale and a number of shared ABM services in addition to SCD. Sunrise was not eligible to become an Interac member in its own right, since it could not meet the eligibility criteria established by Interac. It was also not permitted to establish a "gateway" to the Interac Network. It was therefore unable to pool sufficient numbers of terminals and card holders or to attain the retailer support necessary for a viable new shared EFT network. Sunrise was inevitably abandoned. Two further examples were the Express and Access ATM networks. Express failed in 1986 and Access ATM did the same in 1987 essentially for two reasons: (1) the failure of the Charter Members individually to join these other networks and thereby permit card holders of members of these other networks to utilize ABMs of the Charter Members; and (2) the restrictions imposed by Interac that prevented a gateway, or access to the Interac Network, for these other networks. If Express or Access ATM had been able to directly connect to the Shared Services, this would have provided a competitive alternative for Sponsored Members of Interac to access the Shared Services.

[14] The joint venture aspect of Interac is an important difference from many U.S. networks. McAndrews and Rob (1996) report that three of the ten largest U.S. ATM networks are joint ventures, as are the Visa and MasterCard credit card corporations.

[15] Interac later became the only EFT network in Canada to offer point of sale services. This further ensured the dominance of the Interac Network.

[16] The DOJ argued that "the incremental consumer convenience that would result from admitting the savings and loan association appeared to outweigh the restraint on rivalry that might occur between the two competing networks." In due course PULSE became the dominant network in Texas.

[17] The recent debate in the *Antitrust Law Journal* between D. W. Carlton and A. S. Frankel (1995a) and (1995b) and D. S. Evans and R. Schmalensee (1995) reveals the wide range of positions taken by economists on the issue of access to joint ventures.

[18] See Interac, *supra*, note 1 at 28 to 33.

[19] Mathewson and Quigley, *supra*, note 1 at 21.
[20] Membership in the CPA is restricted by statute, (*Canadian Payments Association Act*, R.S.C. 1985, c. C- 21, s. 30).
[21] An example of a sweep account is described *supra*, note 7, in the discussion of the GMAC/Royal Trust arrangement.
[22] In the Reason For Consent Order, the Tribunal stated: " Until the CPA acts, non-FIs and FIs alike will be unlikely to commit to any indirect access arrangements given the cost of disrupting the arrangement. The CPA may choose never to act. Or it may impose restrictions that limit permissible sweeps to Type 1. In either case, the DCO provision removing the prohibition against sweeps from Interac will have no effect."
[23] CPA paper, "Sweep Account and Payable-through Arrangements: Risk-related Issues and Possible Mechanisms to Address Them," August 1997.
[24] Mathewson and Quigley, *supra*, note 1 at 19.
[25] *Globe and Mail*, January 13, 1998.
[26] Interchange fees are not levied on an Interac direct debit (POS) transaction.
[27] We say this because pressure may mount within Interac to reduce the interchange fee, particularly if it is perceived as encouraging "business stealing" entry.

---

# COMPETITION AND TRADE POLICY IN THE GLOBAL ARENA: AN INTERNATIONAL BUSINESS PERSPECTIVE*

## INTERNATIONAL CHAMBER OF COMMERCE REPORT ON THE PARIS, CONSULTATIVE FORUM, 21 FEBRUARY 1998

By: Crystal Witterick, Davies, Ward & Beck, Toronto
Member, Coordinator and Rapporteur
of the ICC Joint Working Party on Competition and International Trade

### A. Introduction

Globalization and international progress in reducing tariff barriers has resulted in an increasing focus on the potential for both government-imposed and private anti-competitive restraints to create barriers to international trade.

The ICC, a world business organization founded in 1919 which represents thousands of member companies and associations from over 130 countries,[1] has recognized that there are business concerns about the potential for this type of conduct to impede market access.[2]

Further, businesses have also expressed concerns about (i) the extraterritorial application of antitrust laws, and (ii) adequate protection for confidential and competitively sensitive business information in the face of increased cooperation among antitrust agencies seeking ways to address anti-competitive conduct which spans borders.

With the objective of identifying and addressing from a business perspective the core issues arising from the increasing linkages between trade and competition policy, the ICC established in 1995 a Joint Working Party on Competition and International Trade. This is a Joint Working Party of the ICC's Trade and Competition Commissions, composed of a broad range of individuals from different countries with expertise in trade and competition policy. The Joint Working Party includes representatives from the business and legal communities, as well as a number of observers from respected academic and international institutions such as the World Bank.[3]

The Joint Working Party's mandate is particularly timely and relevant given the increasing attention to these issues, and the current agenda of the WTO Working Group on Competition and Trade.[4]

In a Policy Statement issued by the ICC prior to the 1996 Singapore Ministerial,[5] the ICC encouraged the WTO to support continued analytical work on these issues at the OECD in close consultation with business. The Policy Statement also suggested that "an understanding of the linkages between competition and trade had not developed sufficiently to determine how the issues involved might be tackled in a multilateral negotiation, and that at the present time, the WTO Ministerial should limit its work in this area to an examination of how and to what extent competition policy issues should be included on the WTO's future work agenda".

International businesses are concerned that business interests be addressed in this process. The study of these issues should not be diverted by academic debate or based on consultations which are solely among government officials without consideration of relevant business perspectives.

**B. Draft Report of the Joint Working Party and the Consultative Forum**

After identifying the key issues, the Joint Working Party allocated its work among five sub-committees addressing the following areas:

Convergence of Competition Policies;
Competition and Trade Policy Conflicts;
Antidumping and Competition Law and Policy;
Competition Policy and Market Access; and
- Forum for Addressing Conflicts between Trade and Competition.

Each sub-committee was responsible, through a coordinator, for drafting a chapter on the subject matter assigned to it. The objective of the draft Report was to identify, from a business perspective, the appropriate framework for analyzing the relevant issues which arise in the context of each chapter and present the various viewpoints.[6]

In developing the draft Report, it became apparent that a number of these issues are controversial even among business representatives. It is hoped that the draft Report will provide a framework for consideration of these issues by government, business and academic organizations to assist in focusing future discussions and debate.

This draft Report was presented at the Consultative Forum held in Paris on 21 February 1998. The input from the Forum will be considered before finalizing the draft Report. The remainder of this Summary Report provides an overview of the key viewpoints discussed at the Forum.

## C. Overview of Issues Discussed at the Consultative Forum

### 1. Business Concerns

In the context of increasing trade liberalization, business representatives expressed a desire for the right to compete, free from discrimination, in foreign markets. They also seek certainty and efficiency with respect to the enforcement of competition laws, including the identification of clear-cut safe harbours.

Business representatives also expressed concerns about adequate protection for confidential and competitively sensitive information in the face of greater cooperation among competition authorities in response to enforcement problems associated with increasingly global business transactions.[7]

However, it became apparent from the discussion that competition policy is not the only issue for business. A number of other barriers to entry and effective competition were identified, including investment laws, taxation and other domestic regulatory policies. Some commentators expressed the view that there is perhaps an over-emphasis on the role of competition policy in addressing market access issues, but it was noted that this depends on whether you define competition policy broadly or narrowly.

There was general agreement that there are state-imposed barriers to free competition but some expressed the view that these are a matter of sovereign prerogative. In addition to state barriers, there may be private anti-competitive conduct which raises barriers to effective foreign entry, although again, this view is not unanimous.

There are a number of public regulatory policies which affect all businesses. In addressing these issues, it was remarked that businesses want a new approach; not necessarily one policy and not necessarily a global one. Businesses should be able to operate efficiently on a global basis. This objective is impeded by public policies which have not developed within a coherent framework, both within states and on an international level. It was noted that if this were the state of affairs within a company, the company would not survive for very long. Accordingly, the development of a plan to address these issues was supported.

### 2. Conflicts and Convergence

It was noted that while the ICC supports increased convergence to facilitate a level playing field for business, there is no consensus as to what standard convergence should be directed. Skepticism about the benefits and practicalities of broad-based convergence, even assuming this is a desirable objective, was expressed given that states have different economic and cultural objectives in developing policies and enforcing laws, and that states are reluctant to liberalize sectors considered vital to their economies.

As reported below, it was recognized that there is a need to discuss what can be done to reduce frictions which arise as a result of conflicting policies and the manner of enforcement of those policies, while recognizing there are differing views on the issues.

It was noted that in a true global economy, competition policy and trade policy may converge, but that we are not there yet. However, incremental convergence was identified as a possible goal, which could be achieved by starting slowly and focussing on similarities, not differences, in policy and laws. It was also suggested that increased cooperation between states, at least with respect to competition policy, will lead to convergence. This generated a discussion about business concerns about information sharing among antitrust agencies without appropriate safeguards.[8]

Suggestions were also made that some of these frictions may be caused by a misunderstanding about the terminology used when discussing these issues, and that accordingly, it would be useful to define the relevant concepts, such as convergence, market access and market contestability. It was suggested that the OECD may provide a useful function in this regard.

It was generally agreed that one key issue is where to find a balance between the interests of government and the private sector.

### 3. Antidumping and Competition Law and Policy

There was a lengthy discussion about the role of antidumping laws in trade liberalization, and it was noted that without this remedy, it is difficult to succeed in negotiating away trade barriers given the frictions which inevitably arise. In this sense, antidumping laws are a safeguard measure to pave the way for increased trade liberalization. Accordingly, it was advocated that antidumping remedies must remain available until world markets are sufficiently integrated. It was suggested that antidumping laws are the only instrument available to counteract unfair trade practices and that the WTO framework offers a sensible approach to protect against abuses.

However, the view was also expressed that it is time to repeal or modify the antidumping laws, for example, by tempering them with competition policy rules in order to protect abuses. Concerns were expressed about the potential for antidumping regimes to be used as protectionist measures and seriously restrict import

competition. In this context, a number of preconditions necessary to replacing antidumping laws with competition laws were identified, including the existence of minimal tariff barriers, comparable or harmonized competition law regimes, the recognition of jurisdiction based on effects, and adequate private rights of action. Others expressed skepticism that even if this is a desirable objective, it is not practically possible.

In any event, it was generally accepted that to the extent there continue to be antidumping laws, it is important that they offer a quick, effective remedy narrowly targeted at the harm. It was noted that compliance with antidumping rules is usually very onerous and the mere filing of a case can result in substantial market disruption, and that the remedy can be broader in scope than the product which initially prompted the case.

**4. Competition Policy and Market Access**

The discussion began with the comment that firms need meaningful market access to compete globally and that it is no longer sufficient to focus on traditional barriers. In this context, market access involves not only the reduction of barriers to entry, but the ability to compete effectively once entry is achieved (characterized as market presence, although it was noted that market presence does not necessarily mean market share). Broadly defined, competition policy was identified as one tool for facilitating market access, particularly the market presence element.

The other view expressed in this regard was that "market access" really means the use of competition policy to facilitate the opening of markets and that this is not an appropriate objective. Market access is essentially the same as trade liberalization and competition is only a secondary consideration there is not sufficient evidence that competition policy is necessary to achieve market access. The terms of market access are largely dictated by domestic regulatory policy, not competition policy (again, however, it was noted that this conclusion depends on how narrowly you define competition policy).

Further, because national competition laws and enforcement are local matters and will reflect the economic and other objectives of governments, they should be dealt with separately from the concept of market access. For example, it was noted that one issue cited as a barrier to market access is the granting of exemptions from competition policy for specific industries; however, it must also be recognized that developing countries may need to protect indigenous industries. Accordingly, in light of the different objectives of competition policy, it should not be used to extraterritorially achieve market access. While it was recognized that trade and competition policies may converge in a truly global market, this is not the current state of affairs.

It was remarked that what businesses seem to be seeking is a level playing field, characterized by openness, equality of access and nondiscrimination. These objectives could perhaps be addressed in part through the application of general principles of free and open trade. This could involve the application of competition policies, which is a broader concept than competition laws.

There was also significant discussion about the potential impediments to trade from private restrictive business practices. Some expressed the view that as trade is liberalized, businesses seek other measures to protect their market position, and the problem of international cartels is too important to ignore. However, others argued that there is no evidence that private business practices can restrict international trade (versus domestic competition).

A third view offered was that perhaps some of these frictions will be resolved through a rationalization of all policies, i.e. trade, competition, investment and other regulatory policies.

It was generally agreed that a clearer definition of terms would be useful in framing further debate on these issues, and that it would be helpful to compile evidence supporting the various positions.

**5. Forum for Resolving Disputes**

The issue of whether there is merit, at this time, in considering a multilateral forum for dispute resolution with respect to issues arising from the interface between trade and competition policy was the subject of an animated debate. It was evident that there is no clear-cut, universally agreed upon mechanism to address these issues. A number of approaches were identified, which could be pursued either contemporaneously, or in the alternative. These include:

(i) continued analytical work by the OECD and other governmental and business organizations;
(ii) increasing bilateral and multilateral cooperation to promote convergence and reduce friction;
(iii) the incorporation of competition principles within the WTO framework; and
(iv) the adoption of minimum standards or a multilateral competition code.

The debate focused on what is realistic within present structures. It was generally agreed that further education, analysis and dialogue would be productive. Some expressed skepticism about the benefits and practicalities about broad-based convergence. Concerns about the sharing of information among competition authorities were reiterated.

The OECD was identified as a promising forum given that its members have fully developed competition laws and it provides the opportunity for the greatest possible consensus. However, it was noted that the OECD does not have a dispute settlement mechanism and only limited membership.

The reasons why some felt that a multilateral code is premature were debated. These reasons include the fact that there is a wide disparity in competition laws among countries and that some countries do not even have competition laws. Others suggested that a general framework agreement, rather than a substantive body of rules, might be feasible.

The merits of the WTO as a useful forum to address these issues, at least beyond further study, were discussed. It was noted that the WTO lacks experience in this area and many of its members have only basic competition laws, if any at all. Doubts were also expressed by some about the feasibility of using the WTO dispute resolution mechanism in the context of these issues.

On the other hand, a number of reasons were identified in support of going forward at the WTO level, including the coherence of the trading system, the considerable trade experience and near universal membership, the fact that it responds to the interests of both the developed and developing countries, and the availability of a model for dispute resolution.

These are key issues confronting business and governments, and business views are still evolving. Given the significant debate on these issues and the wide divergence of views, it seems that the time is not yet ripe to develop international competition policy disciplines in the context of the WTO. There is much work to be done before a sufficient consensus can be achieved among governments and stakeholders with respect to international negotiations concerning the relationship between trade and competition policy.

### D. Need for Further Dialogue

If such a consensus evolves, it will only occur through analytical and educational initiatives such as the Consultative Forum and in other international fora. It is essential that governments and international organizations encourage dialogue with all stakeholders, including international business, regarding the relationship between trade and competition policy. Just as in the domestic economic policy arena where consultations with business stakeholders are essential for the development of an informed, realistic and effective policy, the same is equally true at the international level.

**Notes**

[1] The ICC's purpose is to promote international trade, investment and the market economy system. Business leaders and experts drawn from the ICC membership establish the business stance on a wide range of international policy issues, including trade, investment, competition, environment, financial services, information technologies, intellectual property, marketing ethics, taxation, telecommunications and transportation.

[2] ICC Policy Statement on "Trade and Competition Policy" prepared by the Commission on Law Practices Relating to Competition, Document no. 225/465 Rev. (22 October 1996).
The ICC Programme of Action for 1996 states that: "It is no longer sufficient to focus on 'trade' barriers as the primary impediment to doing business across frontiers. Instead, the focus must increasingly shift to a wider conception of market access - to the international rules for doing business on a global basis." The ICC has also taken the position that: "trade liberalization is further obstructed from achieving its goal of free market access when governments and enterprises inhibit market contestability through a range of practices which may be considered as falling within the ambit of competition policy. Frequently those practices discriminate against newcomers both foreign and domestic seeking to supply goods and services. Certainly, the global marketplace for business is significantly distorted by a considerable diversity of national practices and laws relating to competition - and of national approaches to enforcing such laws."

[3] The ICC Joint Working Party is chaired by Calvin S. Goldman, Partner, Davies, Ward & Beck.

[4] Singapore Ministerial Declaration, World Trade Organization, Ministerial Conference, Singapore (31 December 1996).

[5] ICC Policy Statement, "Trade and Competition Policy".

[6] The views expressed in the draft Report are not necessarily those of the coordinators and sub-committees for each chapter; rather they reflect input from other members of the Joint Working Party and from ICC National Committees. The draft Report has considered the policy positions taken into account by other organizations such as the Business and Industry Advisory Committee ("BIAC"), the Organization for Economic Co-operation and Development ("OECD"), the Transatlantic Business Dialogue (the "TABD") and the United Nations Conference on Trade and Development ("UNCTAD"). Although there is necessarily some degree of overlap in certain aspects of the chapters, an effort has been made to minimize repetition and inconsistencies. This effort will continue before the Report is finalized.

[7] These concerns are discussed in the ICC "Statement on International Cooperation between Antitrust Authorities", ICC Commission on Law and Practices Relating to Competition, Document No. 225/450 Rev. 3, (28th March 1996).

[8] See ICC Policy Statement, "Trade and Competition Policy", Prepared by the Commission on Law and Practices Relating to Competition, Document No. 225/465, Rev. no. (22 October 1996).