TAMING OLIGOPOLIES THROUGH COMPETITION LAW*

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The passage of the Philippine Competition Act[1] ("PCA") has been hailed as a game changer for the Philippine economy, while the Philippine Competition Commission ("PCC") has been described by legal luminaries as a "superagency" vested with significant powers to perform its broad mandate. More recently, the press has called PCC "the Ombudsman of the market"[2]—ensuring integrity in the private sector while at the same time promoting transparency and accountability in the public sector.

There is much to discuss about this recent legislation. Competition Law, which is also called *antitrust* in the United States, is a critical part of the movement of "Law and Economics" in foreign jurisdictions.

My presentation will cover three broad areas. *First*, I'm going to talk about the economic benefits of competition and provide some demonstrative facts and figures. *Second*, I'm going to briefly discuss the history of competition in the country. And *third*, I'm going to highlight certain aspects of the PCA which may be of interest to you.

Let me frame the presentation by starting with a very basic point.

The overconcentration of wealth is a concern of sufficient importance that no less than the Constitution addressed this issue by codifying a social justice provision mandating that the State reduce

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[1] Rep. Act No. 10667 (2015) [hereinafter "PCA"]. The Philippine Competition Act.

[2] Doris Dumlao-Abadilla, *PCC teams up with Ombudsman*, PHIL. DAILY INQ., June 19, 2017, *available at* http://business.inquirer.net/231615/pcc-teams-ombudsman.

economic inequalities and diffuse wealth for the common good.[3] As early as 1987, the Filipino people understood that when the fruits of the economy are apportioned only among a few oligopolies, state intervention becomes necessary to temper economic inequality.

Fortunately, our Charter's framers did not leave us defenseless against the accretion of economic power in the hands of the few. To keep such power in check, they crafted the Constitution's competition provision. Article XII, Section 19 provides: "The State shall regulate or prohibit monopolies when the public interest so requires. No combinations in restraint of trade or unfair competition shall be allowed."

Broad as it is, the provision has been invoked and applied by the Supreme Court in a few cases. But while the provision can have a strong nullifying function—the Supreme Court has nullified the Downstream Oil Industry Deregulation Act of 1996 based on this provision[4]—it leaves much to be desired in terms of compelling the various instrumentalities of the government to adopt positive measures to promote and ensure effective market competition. Competition enforcement, then, was largely fragmented and uncoordinated, resulting in conflicting policies. There was no single government authority primarily tasked with regulating business through a competition lens.

After more than 20 years in Congress since the filing of the first comprehensive bill on competition, the PCA was finally enacted. Its Declaration of Policy emphasizes that "the provision of equal opportunities to all promotes entrepreneurial spirit, encourages private investments, facilitates technology development and transfer and enhances resource productivity."[5] It also recognizes that an unencumbered market competition allows consumers to exercise their right of choice over goods and services.[6]

But we start off with a basic question. What is competition?

You will not find a definition of "competition" in the PCA, nor in its Implementing Rules and Regulations ("IRR"). But some kind of explanation is in order.

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[3] CONST. art. XIII, § 1: "The Congress shall give highest priority to the enactment of measures that protect and enhance the right of all the people to human dignity, *reduce social, economic, and political inequalities, and remove cultural inequities by equitably diffusing wealth and political power for the common good.*" (Emphasis supplied.)

[4] *See* Tatad v. Secretary of Energy, G.R. No. 124360, 281 SCRA 330, Nov. 5, 1997.

[5] PCA, § 2.

[6] § 2.

If you recall basic economics, the term "perfect competition" refers to a market where there are many sellers and buyers, where no one—whether buyer or seller—can influence prices, and where there are no barriers to entry or exit. On the other hand, the complete absence of competition—a monopoly—is where there is a single seller. Hence, perfect competition, while unrealistic, serves as a useful theoretical benchmark in assessing an industry.

Safeguarding competition will maintain opportunities for all to compete so that incumbent market leaders cannot exclude potential entrants who might be able to lower prices, improve product quality, offer consumers more choices, or spark innovation in the market.

What is the importance of preserving a competitive playing field for market players?

Competition is ultimately about market outcomes; how markets perform with respect to prices, choices, and quality. If there is competition in the market, we can expect low prices, new products, more choices, and higher quality. Anything that substantially prevents, restricts, or lessens competition is "anticompetitive." Significant harm must have been caused on prices, quality, and choices available.

We can distinguish between two types of competition effects: there are "direct effects," as well as "dynamic effects."

Direct effects of competition are the immediate effects. For example, when there is healthy competition among firms, we would expect that prices of goods or inputs to production are reasonably low. Another direct effect refers to those that win when they compete. Competition forces firms to use resources more efficiently; or sometimes push inefficient firms out of business. Winners experience an increase in incomes in those markets where inefficiencies have been eliminated as a result of competition.

Dynamic effects are those that arise over longer periods of time, such as increased innovation among firms as a way to deal with intensified competition. With increased innovation, quality of products improves; new products are introduced, giving consumers more choices. When there are fewer barriers to entry, and when abuse of dominance is penalized, small and medium scale enterprises ("SMEs") find it easier to thrive. A more level playing field encourages SMEs. Lower prices for raw materials and inputs also make small businesses more viable.

Both direct and dynamic effects can help reduce poverty. With lower prices of commodities, real incomes increase; households, in turn, have greater purchasing power.

If competition law is effectively enforced, will eliminating anticompetitive conduct actually reduce prices in a substantial way?

One study assembled data from more than 200 major hard core cartels prosecuted in more than 20 developing countries from 1995 to 2013 to see how much extra money consumers had to pay relative to the competitive benchmark when the suppliers of the goods engage in cartel behavior. It was found that overcharges can be as high as over 40 percent. For these selected sectors and countries, the average overcharge is about 25 percent, which is substantial. It is in fact higher than the effective income tax rate.[7]

Studies show that poorer households stand to benefit more from competition than richer ones. The intuition is that staple goods constitute a large share in poorer households' total budget, so that the price reductions due to competition enforcement and pro-competitive government policies have a relatively larger impact on poorer households.[8]

Moreover, competition authorities for various reasons could also prioritize and take more seriously enforcement in imperfect markets for basic goods. Thus, overall, competition law enforcement outcomes tend to be larger for the poor. For example, in South Africa, competition enforcement in basic sectors brought greater benefits for poorer households because these basic sectors constituted 15.6 percent of total expenses, compared to less than 2 percent for the richest households.[9]

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[7] Aleksandra Khimich, Marc Ivaldi & Frédéric Jenny, Measuring the Economic Effects of Cartles in Developing Countries (May 2014) (research project funded by the Centre for Economic Policy Research Private Enterprise Development in Low-Income Countries, submitted to the UN Conference on Trade and Development), *available at* http://unctad.org/en/PublicationsLibrary/ditcclpmisc2014d2_en.pdf.

[8] Sara Nyman & Martha Martinez Licetti, *Competition and poverty: How far have we come in understanding the connections?*, WORLD BANK BLOGS, May 18, 2016, *available at* https://blogs.worldbank.org/psd/ppps/competition-and-poverty-how-far-have-we-come-understanding-connections.

[9] WORLD BANK GROUP, *South Africa Economic Update: Innovation for Productivity and Inclusiveness* (2017), *available at* http://documents.worldbank.org/curated/en/779551505322376708/pdf/119695-WP-PUBLIC-SA-EU-2017-Digital-Version-Sep-19.pdf.

What were the baseline competition conditions at the time the PCA was passed into law?

The manufacturing sector has been characterized by scholars as "highly concentrated."[10] Concentration ratios refer to the share of the largest firms in an industry. For example, a CR4 of 100 percent means that the 4 largest firms in an industry account for 100 percent of all sales in such industry.[11] A study in 2002 indicates that roughly two-thirds of the manufacturing sector have concentration ratios ranging from 70 to 100 percent.[12]

What this means is, unfortunately, not easy to interpret. On one hand, high concentration could suggest collusive and abusive behavior. On the other hand, high concentration could also mean greater efficiencies and superior market performance that bigger companies can deliver, particularly, when economies of scale are taken advantage of.

In another recent study, it was found that industries that are less concentrated are also those where employment growth is higher.[13] This is consistent with the idea that competition has dynamic effects. Competition makes businesses act in a way that causes production to increase, and thus, requiring more manpower.

In the 1980s, major reforms had been implemented to address a highly restrictive and regulated economy—an economy that clearly lacked competition—in both the domestic and foreign sectors. Such lack of competition had generated huge inefficiencies. The reforms included a series of trade liberalization measures, including the lowering of tariff rates and removal of import controls. We had slowly progressed from a protectionist system to a relatively open-trade regime. Tariffs went down across sectors from highs of 100 percent (or even more) before 1980 to 3 to 10 percent for the majority of products by early 2000.[14]

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[10] Rafaelita Aldaba, *The State of Competition in the Philippine Manufacturing Industry*, Philippine APEC Study Center Network Discussion Paper 2000-13 (2000), *available at* https://pascn.pids.gov.ph/files/Discussions%20Papers/2000/pascndp0013.pdf.

[11] *Id.* at 10.

[12] *Id.* at 22.

[13] Rafaelita Aldaba, *Assessing Competition in Philippine Markets*, Phil. Inst. for Dev. Stud. Discussion Paper Series No. 2008-23 (2008), *available at* https://dirp4.pids.gov.ph/ris/dps/pidsdps0823.pdf.

[14] *See* Erlinda Medalla, *Trade and Industrial Policy Beyond 2000: An Assessment of the Philippine Economy*, Phil. Inst. for Dev. Stud. Discussion Paper Series No. 1998-05 (1998), *available at* https://dirp3.pids.gov.ph/ris/pdf/pidsdps9805.PDF.

Apart from trade reforms, other reforms that had an impact on the state of competition in the Philippine economy beginning in the 1980s include: privatization, de-monopolization of the telecommunications industry, deregulation in the shipping and airline industries, oil deregulation, easing of entry of foreign banks, adjusting the foreign equity limits, and resorting to a much less restrictive negative list of activities where foreign equity is limited.

We can briefly look at the experience in one sector, the airline industry, where competition has been enhanced by deregulation. But before that, we need to go again into a little economics. The gap between the price and marginal cost or the competitive benchmark is called the price-cost margin ("PCM") which is a measure of market power. The higher this is, the market is possibly less competitive.

Prior to 1995, there was a single carrier, Philippine Airlines. The PCM was estimated by a study at 67 percent. In 1995, Executive Order No. 219 was issued, which deregulated the air transport industry, and eliminated restrictions on domestic routes and frequencies, as well as government controls on rates and charges. At around this time, more players entered the market, including Cebu Pacific, and the PCM dropped to 52 percent. It further dropped to 49 percent in 1997. Latest studies by our team have estimated that it has even come lower than 49 percent. The reduction in margins can be attributed to the substantial competition that resulted after the deregulation of the industry.[15]

Another example is the telecommunications sector, which was dominated by a private monopoly, the Philippine Long Distance Company, for more than half a century. For those of you old enough like me, recall those times when we had to wait for decades for a line, and when you do get a line, you also get a party line with it. The sad state of affairs during this period was immortalized in Lee Kuan Yew's statement that: "Ninety-nine percent of Filipinos are waiting for a telephone and the other one percent for a dial tone[.]"[16]

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[15] Rafaelita Aldaba, *The Impact of Market Reforms on Competition, Structure and Performance of the Philippine Economy*, Phil. Inst. for Dev. Stud. Discussion Paper Series No. 2005-24 (2005), *available at* http://www.eaber.org/system/tdf/documents/PIDS_Aldaba_2005_02.pdf?file=1&type=node&id=22306&force=.

[16] Lee Kuan Yew, Speech delivered at the Philippine Business Conference, Manila, Philippines (Nov. 18, 1992), *available at* http://stars.nhb.gov.sg/stars/public/viewPDF-body.jsp?pdfno=lky19921118.pdf.

The telecommunications sector was liberalized in the late 1980s. The reform process accelerated with the implementation of substantial policy changes in the early 1990s. In 1992, the cellular mobile service was liberalized. In 1993, Executive Order No. 59 mandated the interconnection of all carriers, while Executive Order No. 109 opened the basic telephone service to new entrants. These changes, together with the enactment of Republic Act No. 7925 or the Public Telecommunications Policy Act of 1995, led to the de-monopolization of the telecommunications industry. The de-monopolization led to cheaper calls and SMS. From a high of USD 2 per minute before the liberalization, the charge for IDD call for landlines has significantly declined.[17]

Some of you may have come across news items on our ongoing dispute with the telecom duopolies—Smart and Globe—involving one of the biggest transactions in the industry, valued at almost PHP 70 billion for the purchase of the telecom assets of San Miguel Corporation. Since this matter is now pending with the Supreme Court, I would refrain from discussing the merits of the case except to say that the PCC will continue to assert its authority and mandate to make sure that there is competition in the telecom sector, and the consumers are protected.

So now we turn to the metes and bounds of the statute.

Among its salient provisions is the creation of an implementing agency. The PCC is an independent, quasi-judicial body. It has original and primary jurisdiction over all competition-related issues in trade, industry, and all commercial economic activities.

What exactly is the role of the PCA in promoting competition?

The law penalizes anticompetitive agreements, abuse of dominance, as well as anticompetitive mergers and acquisitions.[18] The prohibition applies to private firms as well as government-owned or controlled corporations.[19] An assessment of a potential violation is done on a case-by-case basis. Evidence has to be provided for every alleged breach of the law. There is no general rule that bigness or monopolies or high concentration is

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[17] Ramonette Serafica, *Competition in Philippine Telecommunications: A Survey of the Critical Issues*, Center for Business and Economics Research and Development Working Paper Series 2001-01 (2001), *available at* http://www.dlsu.edu.ph/research/centers/cberd/pdf/papers/Working%20Paper2001-01.pdf.

[18] PCA, § 2(c).

[19] § 4(h).

automatically punished; efficiencies that could arise out of such bigness need to be carefully considered. But cartel agreements are *per se* violations.[20]

To implement the law's mandate, the PCC is vested with three main powers, namely: enforcement, merger review, and advocacy.[21]

As regards its enforcement powers, the PCC has the sole and exclusive authority to initiate and conduct a fact-finding or preliminary inquiry for the enforcement of the law based on reasonable grounds.[22] There are three ways by which investigation may be commenced: the Commission may conduct an investigation *motu proprio*, or upon the filing of a verified complaint by an interested party, or upon referral by a regulatory agency.[23]

There are four main types of agreements that are penalized under Section 14 of the PCA: price fixing, bid rigging, output restriction, and market allocation. Price fixing is defined as "restricting competition as to price, or components thereof, or other terms of trade."[24] Bid rigging means "fixing price at an auction or in any form of bidding including cover bidding, bid suppression, bid rotation and market allocation and other analogous practices of bid manipulation."[25] Output restriction refers to the "setting, limiting, or controlling production, markets, technical development, or investment."[26] Market allocation means "dividing or sharing the market, whether by volume of sales or purchases, territory, type of goods or services, buyers or sellers or any other means."[27]

These violations are further classified into the *per se* category, and those that are subject to the so-called "rule of reason" test. The key difference between the two types of prohibitions lies in the mode of analysis. *Per se* violations are those which Congress, in the exercise of its discretion, and on the basis of tried and tested economic theory, has determined to be injurious to competition, and thus cannot be justified by claims of efficiency gains. As regards non-*per se* violations, the analysis must consider the specifics of the challenged conduct and its impact upon the marketplace. Normally, the fact-finder would weigh the circumstances of a

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[20] § 14.
[21] § 12.
[22] § 31.
[23] § 12(a).
[24] § 14(a)(1).
[25] § 14(a)(2).
[26] § 14(b)(1).
[27] § 14(b)(2).

case in deciding whether a practice imposes an unreasonable restraint on competition.

We now turn to abuse of dominant position. I would like to emphasize that being dominant is not wrong or unlawful. A dominant position can be achieved through legitimate means, for example, by developing or selling better or superior products. Moreover, some firms may very well have attained a dominant status because of extensive research and development or strategic marketing techniques. What the law prohibits is the abuse of such dominance.

A firm is in a dominant position if it has the ability to behave independently of its competitors, customers, suppliers, and ultimately, the final consumer. An obvious example is a monopolist—an entity that controls all of the market for a particular good or service. Under the law, however, an entity need not have a 100 percent control of a relevant market to be considered dominant. The PCA, for instance, provides a rebuttable presumption of market dominance if the market share of the entity in the relevant market is at least 50 percent.[28] Nevertheless, even an entity without such control may still be regarded as dominant if it has a significant and durable market power—that is, a long-term ability to raise prices or exclude competitors.

Therefore, if a supplier can arbitrarily increase the price without having to worry about declining sales, or worry about customers switching to other suppliers or product, it most likely enjoys dominant position even if it only has less than 50 percent of the relevant market. Under Section 15 of the PCA, the following acts, among others, constitute an abuse of dominant position: *predatory pricing*, or the act of selling goods or services below cost with the object of driving competition out of the relevant market; *tying*, or the act of making supply of particular goods or services dependent upon the purchase of other goods or services from the supplier which have no direct connection with the main goods or services to be supplied; *refusal to deal*, which includes contracts imposing conditions not to deal with competing entities; and *price discrimination*, which means setting prices or other terms or conditions that discriminate unreasonably between customers or sellers of the same goods or services.

Agreements that are anti-competitive may be restrained by the Commission. Additionally, violators can be levied a hefty administrative fine, which could range from PHP 100 million to PHP 250 million, and a

[28] § 27(g).

criminal penalty, from two to seven years imprisonment.[29] Such sanctions can greatly alter market dynamics. Faced with the prospect of stiff penalties, it is hoped that big players will be dis-incentivized from committing unfair practices.

Having due regard to the fragility of the lower income households, our legislators provided for a sort of aggravating circumstance when the anti-competitive conduct involves basic goods like rice, corn, bread, fresh, dried and canned fish and other marine products, fresh pork, beef and poultry meal, fresh eggs, coffee, sugar, cooking oil, laundry soap, detergents, and firewood. When any of these products are the subject of the violation, the fine is tripled.[30]

We now turn to the PCC's merger review powers.

The PCC has the power to review mergers and acquisitions, including joint ventures, having a direct, substantial, and foreseeable effect on trade, industry, or commerce in the Philippines. Merger analysis predicts a merger's competitive impact whether the proposed merger is likely to substantially lessen competition in the relevant market, and whether such anti-competitive effects can be counterbalanced by projected efficiency gains from the transaction. The goal is to maintain or restore competition affected by the merger. In addition to the other administrative penalties, an agreement consummated in violation of this requirement to notify the PCC shall be considered void, and will subject the parties to an administrative fine of 1 percent to 5 percent of the value of the transaction.[31]

Finally, the law also recognizes that anti-competitive business conduct or acts in the private sector may have their roots in distortions caused by the public sphere—for example, existing government policies, regulations, measures, or programs. Under the law, the PCC can also weigh in on these matters. Section 12(r) of the PCA lists the following as one of our functions: "Advocate pro-competitive policies of the government by: (1) reviewing economic and administrative regulations […] as to whether or not they adversely affect relevant market competition, and advising the concerned agencies against such regulations; and (2) advising the Executive Branch on the competitive implications of government actions, policies and programs."

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[29] §§ 29-30.
[30] § 41.
[31] § 17.

In sum, the tasks of the PCC are legion, the challenge great, and the mandate crucial.

When I joined a little over a year ago, the challenge was to help build the new agency from the ground up while at the same time deal with already ongoing operational concerns. I am proud to report that your competition commission has been very busy, very productive in its first year—setting records of sorts. Consider the following examples.

In just six months, we were able to issue our IRR, a feat probably unmatched by any other agency. We have opened our merger review procedures from the get go. As of last count, we have zero backlog and have completed reviews of 102 deals with a total aggregate value of over PHP 1 trillion. We have also led the drafting of a National Competition Policy which constituted a stand alone chapter in the 5-year Economic Development Plan issued by NEDA. Quite impressive since this is the first time that competition has become a central concern and priority of the Philippine government. We have commenced several investigations, hired more than 100 employees—young, competent, and passionate staff with impressive credentials and experience. We have developed formal partnerships with other foreign competition agencies, invited numerous experts from jurisdictions, such as Mexico, Israel, the European Union, Australia, and the United States, to share with us their best practices and learning experiences from agency action. Cognizant of the synergies produced by inter-agency cooperation, we executed Memoranda of Agreement ("MOA") with other sector regulators such as the Securities Exchange Commission, Energy Regulatory Commission, and Insurance Commission, among others. Such MOAs set forth salient provisions on referrals, information-sharing, and joint efforts in handling cases. Just recently, we met with representatives of the Ombudsman to discuss joint efforts in addressing cases with both competition and corruption elements.

Let me try to end by addressing the elephant in the room.

Recently, there had been some attacks in the media against the PCC.[32] The source of these attacks has obviously been affected by our vigorous efforts to assert our mandate. Indeed, they have reason to be upset. If PCC is to be effective, it will be necessary that it acts as a disruptive force.

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[32] Jon Viktor Cabuenas, *In light of Globe, PLDT, SMC deal, Balisacan says he'd rather resign than burden the business sector*, GMA NEWS ONLINE, June 1, 2017, *available at* http://www.gmanetwork.com/news/money/companies/612957/balisacan-says-he-d-rather-resign-than-burden-the-business-sector/story/.

It will upset certain kinds of personalities and businesses. In taming oligopolies, there will be serious push-back; there will be hard fought battles; and there will be mixed results—you win some, and you may lose more. But that is the story of regulatory reform. It is slow, it is challenging, but it is necessary.

On a personal level, and this is me speaking as a citizen and an academic, antitrust is really not just about lower prices or consumer welfare. It is in fact about democracy.

Returning once more to the Constitution's social justice provision, the words are stirring: "social, economic, and political inequalities" as well as "equitably diffusing wealth and political power."[33] For as the Philippine experience so painfully demonstrates, the oligopolistic structure of the economy is paralleled by the political dominance of a narrow few.

Unlike other fields of law, Competition Law is not primarily concerned with the maintenance of power. In fact, it is concerned with just the opposite—how concentrated economic power can lead to concentrated political power, and how the economically wealthy enjoy an inordinate amount of political influence, distorting representative institutions like Congress, and co-opting key regulatory government agencies. All you have to look at is who are the major contributors in the electoral campaign of various politicians.

So if we are to keep our Republic, if we are to enjoy the fruits of a true representative democracy, it is essential that equality in economic opportunities should be promoted and sustained. In essence that really is the hidden message in the PCA.

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[33] CONST. art. XIII, § 1.