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## Economic Internationalization and Discretionary Rule-Making in Transatlantic Competition Relations

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Rule-Making in Transatlantic Competition Relations*

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## **Abstract**

This paper employs a cross-level analysis to explore the domestic and international factors responsible for cooperation between the European Union and the United States in competition policy. Economic internationalization interacts with domestic politics in both the EU and the US to create a cooperative outcome. The domestic politics of this international cooperation are simplified with a principal-agent model, in which politicians are the principals and competition regulators are the agents. The paper tests this approach across three bilateral EU-US competition agreements signed during the 1990s: The Bilateral Agreement, the Positive Comity Agreement and the Administrative Arrangements on Attendance..



‘I am proud to say that EU/US cooperation in [competition policy] has become something of a model for transatlantic cooperation generally.’

Mario Monti, European Commissioner for Competition (2001: 2)

## Introduction

The dynamic nature of markets requires vigilant competition policies in order to prevent anticompetitive business activity from undermining the benefits of the free market economy. Not surprisingly, the two largest free market economies, the European Union (EU)<sup>1</sup> and the United States of America (US), rely heavily on competition policy to manage activity in their respective markets. Historically, competition relations between the US and Europe have been largely adversarial, characterized by a reliance on extraterritoriality and unilateral countermeasures designed to protect national interests.<sup>2</sup> As business activity has become increasingly cross-border over the last two decades, the EU and the US have begun to enforce their domestic competition policies in a more active and internationally-oriented fashion. Given historical transatlantic tensions in this policy area, the increased enforcement of domestic competition policies in international markets threatens to increase even further the likelihood that different national interests will come into conflict.

Since the early 1990s, transatlantic cooperation in merger control—a central component of competition policy designed to prevent corporate mergers from significantly reducing competition—has increased considerably. This unexpected increase in cooperation suggests a transition in transatlantic competition relations from the historically adversarial reliance on extraterritoriality and unilateral countermeasures to cooperative bilateralism. This transition to cooperative bilateralism begs the question: Given the increasing internationalization of business activity and historical tensions in transatlantic competition relations, how and why has EU-US cooperation in competition policy increased since 1990?

Because of their tendency to focus on one level of analysis, dominant theoretical approaches from the international relations and comparative politics literatures provide only incomplete explanations for such EU-US cooperation. To overcome these shortcomings, the current study develops a cross-level model that specifies a causal relationship between the dependent variable (EU-US cooperation) and a systemic, independent variable (economic internationalization). The precise effect of the independent variable is then explained by an intervening variable—domestic politics, particularly the preferences of EU and US competition authorities operating under domestic institutional constraints. The study finds that EU-US cooperation in competition policy occurs primarily as ‘bottom-up’ cooperation via the discretionary authority of self-interested competition officials. These findings reveal the means by which international cooperation is developing in a traditionally conflictive and largely domestic policy area, a development that, according to EU Competition Commissioner Mario Monti, may serve as a model for transatlantic cooperation more generally (2001: 2).

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1 The term ‘European Community’ is still legally correct when referring to activities that fall under the rubric of the Single Market (Pillar I), including competition policy. For simplicity, I refer to only the ‘European Union,’ regardless of whether the activity in question is legally subsumed under the competency of the European Community.

2 The adjectives ‘national’ and ‘domestic’ typically describe characteristics of traditional, Westphalian states. While the EU is not a traditional state, for simplicity, the Union’s territorial jurisdiction is referred to as ‘national’ and ‘domestic’ throughout the current study.

## Analytical Concepts

### International Cooperation

The current study requires clarification of two central concepts, the first being *EU-US cooperation*. While few concepts in political science enjoy consensus definitions, the notion of cooperation does boast strong definitional agreement. International cooperation is commonly defined (in political science) as occurring ‘when actors adjust their behaviour to the actual or anticipated preferences of others, through a process of policy coordination’ (Keohane, 1984: 51).<sup>3</sup> Keohane’s general definition of international cooperation clearly applies to the type of behaviour investigated in the current study with two stipulations. First, the current study focuses on an important geographical subsection of international cooperation—bilateral cooperation between the EU and US. Second, the current study investigates cooperation specifically in merger control, not generally across a wide variety of different and analytically separable policy areas.

Keohane’s general definition of international cooperation benefits from more precise specification of possible *types* and *processes* of cooperation. Differentiation among these types and processes is crucial to understanding EU-US cooperation in competition policy.

#### *Types of International Cooperation*

EU-US cooperation occurs as two potential types: Non-discretionary and discretionary. These two types are classified according to the degree of discretion enjoyed by non-elected regulators. On the one hand, traditional conceptualizations of international cooperation are largely non-discretionary, defined as cooperation that occurs between states via formal and binding political agreements. Such cooperation is frequently formalized in treaties, which require ratification procedures and have the effect of domestic law. Non-discretionary cooperation occurs as political agreements because the ‘state’ (i.e., elected politicians) will typically reserve this important sovereign right to sign international agreements for itself.

On the other hand, international cooperation also can occur between actors operating at sub-state levels, such as regulators. This cooperation is considered discretionary when it occurs between regulators and is conducted without direct political involvement. The discretionary authority of regulators comes from the power delegated to them by elected politicians and is based in policy objectives found in statutory law. In order to achieve these objectives, regulatory authorities are allowed to use their own initiative to promulgate rules, guidelines, codes, procedures, etc. In certain cases, regulators can use this discretionary authority to initiate cooperation with foreign regulators.

Provisions for both non-discretionary and discretionary authority can be found in domestic EU and US law. To varying degrees, these domestic laws allow competition authorities to cooperate with their foreign counterparts. In transatlantic competition relations, most cooperation is conducted by regulators via discretionary means.

#### *Processes of International Cooperation*

Keohane argues that international cooperation occurs through ‘a process of policy coordination’. This general process of policy coordination can be disaggregated into more distinct processes. The distinct process investigated in the current study is the initial step formalizing EU-US cooperation in international agreements: rule-making cooperation. Rule-making cooperation, which may be non-discretionary or discretionary, creates the formal basis for increasing contacts between competition

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3 For a discussion of the wide agreement on this definition of cooperation, see Milner (1997: 7).

authorities. Following rule-making cooperation, other useful cooperative (and often discretionary) measures can be devised to enhance the resulting process of policy implementation.<sup>4</sup>

Through rule-making cooperation, the EU and US have entered into three formal cooperative agreements since 1990: the Bilateral Agreement, the Positive Comity Agreement and the Administrative Arrangements on Attendance (AAA). While the Bilateral and Positive Comity Agreements are binding on the signatories, the AAA is a non-binding effort at rule-making cooperation. These three agreements will be discussed in detail below.

## Economic Internationalization

The second analytical concept, *economic internationalization* (EI), resembles the common notion of economic globalization. However, the current study uses the term ‘internationalization’ with the intent of distancing itself from frequent claims in the globalization literature that the phenomenon is occurring globally or making ‘the state’ obsolete.

EI is defined as an expansion of markets from the domestic level to the international level caused by economic liberalization, deregulation and technological development. Such a definition of EI, at least tacitly, also includes the expansion of domestic corporate strategies, activities and organizational structures to the international level. EI has dramatically increased rivalry among firms both within and across national borders, which significantly changes business strategies. A common business response to this new pressure is to pursue internationally-oriented mergers as a means to attain internationally competitive economies of scale and enhance overseas market access with new distribution networks and locally-familiar reputations.<sup>5</sup>

The ability of states to control merger activity with domestic competition policies is being threatened by the increasing internationalization of markets and merger activity. This threat is particularly evident in cases of concurrent jurisdiction where a merger and its effects are not fully located within one national territory.<sup>6</sup> The challenge to domestic competition policies is that as firms engage in internationally-oriented merger activity, they internationalize their production, distribution and management beyond the sovereign territory and national jurisdiction of their respective domestic competition authority. The fact that EU and US merger control laws remain domestic while markets are becoming increasingly transatlantic creates a crucial disconnect between national sovereignty and national jurisdiction.<sup>7</sup> As firms and markets internationalize, states must find ways to correspondingly expand their national jurisdiction or lose their sovereign ability to ensure the public good of fair competition in domestic markets. Thus, as EI changes opportunities and incentives for firms, so too must governments change their behaviour if they wish to control merger activity that increasingly

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4 While the current study focuses on rule-making cooperation, subsequent processes of cooperation may be identified, such as implementation and exploratory institutional cooperation. In competition policy, *implementation* cooperation typically occurs on an informal, case-by-case basis in which competition authorities exchange information and coordinate their investigations in order to reduce the likelihood of conflicting decisions. Implementation cooperation may encourage substantive convergence (e.g., consistent decisions) and procedural convergence (i.e., investigation coordination). After successful rule-making and implementation cooperation, informal efforts at *exploratory institutional* cooperation may emerge as new ways to review and enhance policy implementation.

5 Internationally-oriented merger activity has increased dramatically in the last two decades. For measures reflecting this trend in the 1990s, see UNCTAD (2000, 108). For impact of EI on business strategies, see Evenett *et al.* (2000), Garten (2000), Gaugan (1999).

6 For similar arguments, see Fox (2001: 350), Devuyst (2000: 320-321), Gual (1995: 15), Gerber (2001: 435) and Waverman *et al.* (1997).

7 ‘Sovereignty’ here is understood as the *ability* of states to achieve specific domestic policy outcomes, not the *autonomy* of individual states to act in the international system.

occurs across or outside their national borders but still affects their domestic market (European Commission, 1994: Annex I, 2; Parker, 1999).<sup>8</sup>

Governments can respond to the new threat of EI by extraterritorially imposing domestic merger review authority on mergers occurring in concurrent markets. In such cases, governments must also consider the increasing possibility that foreign competition authorities will intervene in domestic matters by reviewing merger activity occurring in their domestic market. The resulting jurisdictional overlap precipitates contact and, often, political and economic conflict (ICPAC 2000). Governments can respond to the complication of foreign political intervention with a variety of unilateral measures. Such unilateral approaches exacerbate the uncertainties and tensions that follow from overlapping national jurisdictions, increasing the likelihood that national interests and competition policies come into conflict. Historically, transatlantic competition relations have been such reciprocal exercises of extraterritoriality and unilateral retaliation, frequently threatening to escalate into multi-sectoral trade wars (see Section III).

Alternatively, governments can choose to cooperate in an attempt to ensure competitive (domestic and international) markets and avoid the tensions caused by external political intervention in domestic markets. Beginning in the 1990s, the EU and US chose to meet the challenge of internationalizing business activity by cooperating with their counterparts across the Atlantic. This cooperation appears to have largely overcome the challenges presented by EI and overlapping jurisdictions. Yet, while EU-US cooperation in merger control has increased dramatically over the last decade, it is not clear *how* and *why* this cooperation has occurred, especially given the historically adversarial nature of transatlantic competition relations.

### Historical Adversity in Transatlantic Competition Relations

EU-US cooperation in merger control is particularly unexpected given the adversarial history of transatlantic relations in competition policy. Much of the tension that emerged in competition matters was over the development of unilateral extraterritoriality.<sup>9</sup> The US has a long legal history of extraterritoriality in the context of competition policy (Peritz, 1996; Sullivan, 1991), dating from the 1945 Alcoa decision, in which the US Supreme Court developed the ‘effects test’ of subject matter jurisdiction for competition policy.<sup>10</sup> For their part, many European states responded to US extraterritoriality by drafting retaliatory legislation. Most notable among these national countermeasures were the so-called ‘blocking’ and ‘clawback’ statutes, designed to protect European companies from US extraterritorial jurisdiction.<sup>11</sup> The sum result of these institutional developments was a transatlantic game of unilateral extraterritoriality followed by a spiral of countermeasures. These competition relations based on brinkmanship continued through the 1980s.

During the 1980s, additional domestic events in the US and Europe compounded the historical differences and tensions in this policy area. The EU feared an increasingly activist and unilateral extraterritorial US competition policy due to posturing by George H. Bush’s Administration (Brittan, 1990) and the US Congress, such as Section 301 of and the Exon-Florio Amendment to the Omnibus Trade and Competitiveness Act of 1988 (Garbus, 1991: 64; Miles, 1995: 120). In fact, Exon-Florio, which allows the US President to prohibit mergers that threaten national security, was shown to be more than a threat as it was actually used against European firms (Garbus, 1991: 70; Kang, 1997).

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8 For other arguments that elaborate the disconnect between national authority and national jurisdiction due to changes in the international economic system, see Monti (2001a), Monti (2000b), ICPAC (2000), Slaughter (1997).

9 Additional US measures like treble damages in private cases also created significant tensions with overseas authorities (Griffin, 1998: 70).

10 *United States v. Aluminum Co. of America*, 148 F.2d 416 [2d Cir. 1945].

11 On these countermeasures, see Fox (2001: 359) and Griffin (1999, 1998).

For the US, fears were generated by the European Court of Justice's (ECJ) apparent willingness to expand the EU's jurisdictional reach during the 1980s.<sup>12</sup> This new activism was seen in the ECJ's 1988 Wood Pulp decision, which established the Union's extraterritorial jurisdiction.<sup>13</sup> This ruling addressed a competition case that affected North American firms, demonstrating that the EU was not likely to shy away from extraterritorial confrontation over competition issues with the US. From the US perspective, institutional developments within the EU also suggested a maturation of the Union and its potential willingness to exercise extraterritorial jurisdiction in competition matters. In particular, the EU was negotiating the completion of its single market and the establishment of its own Merger Control Regulation (See Section V, 6 below).

During the 1980s, the trend of historical transatlantic adversity in competition relations showed few signs of abating. Rather, EI was increasing the pressures for firms to engage in more cross-border mergers and simultaneously increasing the likelihood of concurrent jurisdictional merger reviews. Based on historical experience, the resulting jurisdictional overlaps would lead to further disagreements and political brinkmanship in transatlantic competition relations.

### Explaining the Cross-Level Politics of Transatlantic Competition Relations

Systemic explanations in the international relations literature typically focus on the behaviour of 'states', at the cost of domestic factors, to explain international cooperation. These explanations accept, to varying degrees, a causal link between the systemic-level EI and international cooperation. Alternatively, explanations found in the comparative politics literature emphasize the importance of domestic factors in policymaking but typically discount the causal impact of systemic-level phenomena like EI. Thus, neither of these literatures offers a satisfying explanation for 1) why EU-US cooperation in competition policy is primarily discretionary, *and* 2) why systemic-level EI initiates EU-US rule-making cooperation in competition policy.

### The Principal-Agent Model of Delegation

To provide a more convincing explanation, the current study introduces a cross-level analysis that considers the causal role of international *and* domestic factors. The cross-level approach focuses on the interaction among a systemic independent variable (EI), an intervening variable (domestic politics) and a dependent variable (international cooperation). More formally, the current study tests the following cross-level model:

↑ EI + domestic politics (i.e., regulatory agent preferences and domestic institutional constraints)  
⇒ ↑ EU-US cooperation in competition relations.

The causal impact of the systemic-level EI on business and government behaviour in merger activity has been detailed above (see Section II, B.). However, to understand better the domestic politics underlying EU-US cooperation in competition policy, the insights of the principal-agent model of delegation (PAM) are incorporated.<sup>14</sup> PAM provides a useful simplification of domestic politics by focusing on the role of institutions and the interests of important actors involved in transatlantic competition relations.

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12 On the development of EU extraterritoriality, see Griffin (1999), Devuyt (1998), Goyder (1998).

13 Cases 89/85, etc., *Ahlström v. Commission* [1988] ECR 5193. On the Wood Pulp decision, see Lange and Byron Sandage (1989).

14 For an overview of the principal-agent model, see Moe (1984). Some of the earliest work on the principal-agent model in political science comes from Mitnick (1980). Other notable examples that address the delegation issues inherent in the principal-agent model include Thatcher and Stone Sweet (2002), Huber *et al.* (2001), Huber and Shipan (2000), Banks and Weingast (1992), Calvert *et al.* (1989), McCubbins (1985), Weingast and Moran (1983).

PAM relies on three central assumptions: 1) different domestic actors engage in rational, utility-maximizing behaviour, 2) politicians and regulators have different preferences, and 3) information asymmetries are crucial to understanding the relationship between politicians and regulators. Political principals delegate regulatory authority on a contractual basis to non-elected agents. After delegating this authority, the elected politicians are faced with the challenge of creating a system that compels the regulatory agents to act in the principals' interest. PAM generally posits an optimistic prediction that politicians are able to maintain a significant degree of control over regulators and, thus, over policy output.

The challenge for principals to control the behaviour of agents is caused by inherent information asymmetries that benefit the agents—principals are not able to observe all the daily activities of the agents due to limited resources and because agents typically know better their areas of expertise. Because principals cannot legislate and observe all agent activities, principals provide agents the authority to engage in certain activities at their own discretion. Discretionary authority allows bureaucratic agents to fill in the gaps of policy implementation that are left when political principals draft broad legislation (Epstein and O'Halloran, 1999: 51). While it is conceivable that political principals could draft very detailed legislation that left no room for discretionary authority, it is unlikely to occur in large, complex regulatory systems like the US and EU that impose multiple demands on political principals.

By providing discretionary authority to agents, political principals can reduce their costs of implementing and enforcing regulatory policy. However, the provision of discretionary authority can also increase the costs of policing regulatory agreements (Majone, 2000: 42). When discretionary authority is broad, agents can expand their decision-making autonomy to produce regulatory outputs that conform to their own preferences. As Majone explains, regulatory agents 'have a strong bargaining position because of their technical and institutional expertise. As a result, they are increasingly able to pursue their objective of greater autonomy' (1996: 72).

Agent pursuit of greater autonomy can cause bureaucratic drift—'the ability of an agency to enact outcomes different from the policies preferred by those who originally delegated power' (Epstein and O'Halloran, 1999: 25). When the preferences of agents differ from those of the principals, the agents can exercise their discretionary authority to pursue their own preferences, a behaviour known as agent 'shirking'. Agents may also succumb to 'slippage', which results when the structure of the initial delegation provides incentive for the agents to pursue activities contrary to the goals of the principals (Pollack, 1998: 220).<sup>15</sup> In order to overcome these inherent problems that arise from information asymmetries and agent discretion, principals must develop mechanisms to ensure their control over agent activities.

According to institutionalist arguments, in order to ensure the democratic accountability of regulatory agents, political principals must have access to a variety of control instruments (McCubbins *et al.*, 1987). These control instruments are embedded in domestic institutional arrangements, or, the power-sharing agreements established between principals and agents. The institutional design of these instruments—and the resulting incentive structures for agents—thus becomes an important determinant of the political control of agents.

The control instruments available to principals are frequently categorized as administrative and oversight procedures. *Administrative* procedures are typically established during the initial delegation of regulatory authority to the agents. These administrative procedures 'define ex ante the scope of agency activity, the legal instruments available to the agency, and the procedures to be followed by it' (Pollack, 1998: 220). After the initial delegation, principals have recourse to oversight procedures. *Oversight* procedures exist as two varieties: monitoring and sanctioning. Monitoring allows principals

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15 For more on shirking and slippage, see Moe (1984). In addition, agents can engage in deceptive behaviour via adverse selection prior to the initial delegation and moral hazard after the initial delegation. These two theoretical concepts are less central to the current study. For a useful discussion of adverse selection and moral hazard, see Moe (1984: 754-756).

to reduce the information asymmetries enjoyed by the agent. Typical monitoring consists of ‘police patrols’ (standing oversight committees) and ‘fire alarms’ (constituent complaints and judicial review) (McCubbins and Schwartz, 1984). Sanctioning provides a broader array of control instruments, including ‘control over budgets, control over appointments, overriding of agency behaviour through new legislation, and revision of the agency’s mandate’ (Pollack, 1998: 220-221). Through these control instruments, it is often argued that political principals can prevent the bureaucratic drift that accompanies agent shirking and slippage. As will be discussed below, the current study is primarily interested in the dynamics of agent shirking.

### **The Logic of PAM, EI and International Cooperation**

The principal-agent dynamic suggested by PAM provides useful analytical insights when applied to international regulatory cooperation. The traditional domestic control instruments identified by PAM can be expanded to include internationally-oriented instruments available to political principals to control the behaviour of foreign regulatory agents.<sup>16</sup>

Domestically, political intervention can encourage regulation that benefits specific, narrow (and often partisan) constituent interests instead of meeting the initial statutory mandate of the regulatory agency. This domestic political intervention can also delay regulatory decisions and reduce the certainty and decision-making authority of regulatory agents. Therefore, regulatory agents closely guard their independence from political intervention. Internationally, intervention may come from foreign political principals. Such extraterritorial attempts at control by foreign political principals can increase the likelihood of international political-economic conflict and again reduce the certainty and decision-making authority of regulatory agents. Both domestic and international politicization—even the perception of politicization—can undermine the credibility of regulatory agents, and in particular, the credibility of a non-governmental, administrative-regulatory agent like the European Commission.<sup>17</sup>

Because of the new realities of EI, different national competition authorities must increasingly review the same merger although they have different information with which to conduct the review process. National competition authorities frequently have better information on firms located within their respective national jurisdiction. This information asymmetry increases the likelihood that the different national competition authorities will undertake divergent analyses that generate conflicting decisions on concurrent jurisdiction mergers. Regulatory agents strive to avoid such conflicting decisions because of the perception they create for political principals. Political principals are likely to perceive conflicting decisions as threats to the regulatory mandate established in domestic statutes (Monti, 2000b: 2; Stark, 2000: 5). They may also perceive such decisions as threats to national sovereignty and/or their domestic constituents’ interests. Threats of this type can precipitate very real international conflicts, including trade wars.<sup>18</sup>

In such cases of conflicting decisions, political principals can intervene domestically with the control instruments familiar in the PAM literature: oversight and administrative procedures. In addition, and more importantly for the current study, political principals can also intervene internationally in the activities of foreign competition agents. These internationally-oriented control instruments occur as non-punitive and extraterritorial measures.<sup>19</sup> Non-punitive control instruments

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16 While the measures that political principals use to intervene internationally are also labeled ‘control instruments’, this does not imply that an international delegation has previously occurred from those political principals to the targeted foreign regulatory agents.

17 See Gatsios and Seabright (1989).

18 As ICPAC argues, ‘When divergence [in decisions] occurs, it is the agencies that must often explain and at times attempt to reconcile their differences. Clashes also may lead to trade wars’ (2000: 41).

19 A fundamental difference exists between the legal enforceability of non-punitive and extraterritorial measures. Non-punitive measures function similar to threats or persuasion because they have no direct legal force behind them.

include public statements (e.g., news interviews, official statements, open letters, non-binding resolutions) and lobbying (e.g., phone calls, faxes, face-to-face meetings). Extraterritorial control instruments include fines, bans on commercial activity, prohibitions of undertakings (for national security, etc.), blocking and clawback statutes and trade sanctions. While domestic control instruments are exercised over domestic competition agents, international control instruments are directed toward foreign competition agents.

### Preferences, Hypotheses and Methodology

In today's EI environment, political principals prefer intervening with control instruments to prevent domestic and foreign agents from shirking (i.e., maximizing their regulatory autonomy) when the costs of that shirking exceed the costs of intervention. The costs of shirking generally exceed the costs of intervention when regulatory independence results in perceived threats to national/constituent interests. This preference is reflected in the fact that political principals have historically intervened with control instruments in transatlantic competition relations when they perceived threats to national/constituent interests (see Section III). Such perceptions of threat are likely to follow from conflicting decisions between competition agents.

For their part, regulatory agents prefer avoiding political intervention because it decreases their certainty and decision-making authority. Thus, regulatory agents prefer maximizing their autonomy as a way to increase their certainty and decision-making authority. The maximization of regulatory autonomy via expansions of non-discretionary authority requires approval by political principals (i.e., change to domestic statutes). Expansions of discretionary authority are less costly (Doern, 1996: 278), because political principals play a smaller role. Thus, given the higher costs of pursuing their preferences via changes in non-discretionary authority, regulatory agents are most likely to pursue their preferences via discretionary means (i.e., shirking).

The PAM literature typically argues that increases in agent shirking will lead to increases in political intervention via control instruments. However, the current study suggests a counter-intuitive argument that as agent shirking increases (via rule-making cooperation) in international competition relations, political intervention (both domestically and internationally) decreases. The result of this decrease in political intervention is an increased likelihood of international cooperation in policy implementation.

Agent shirking increases via discretionary rule-making cooperation in order to cope with the new challenges presented by merger activity in an EI environment. Political intervention decreases because agent shirking for cooperation reduces the likelihood of conflicting decisions that might prompt political intervention. Indeed, agent shirking is the conscious construction (via rule-making cooperation) of a dispute prevention system that dramatically reduces the need for dispute resolution by political principals. In other words, due to agent shirking in transatlantic competition relations, *principals are less likely even to encounter situations in which the costs of no intervention (perceived threats to national/constituent interests) exceed the costs of intervention (exercising any variety of domestic and/or international control instruments).*<sup>20</sup>

The combination of EI with PAM's principal and agent preferences suggests testable hypotheses regarding transatlantic competition relations. The following hypotheses are specific to rule-making cooperation:

(Contd.) \_\_\_\_\_

Extraterritoriality occurs as legally actionable punitive measures exercised from one jurisdiction to change the behaviour of actors in another jurisdiction.

<sup>20</sup> It should be noted that such situations, while unlikely and infrequent, do still occur in policy implementation cooperation, such as the 1997 Boeing/McDonnell Douglas merger. A similar exception in rule-making cooperation—the discretionary pursuit of the 1991 Bilateral Agreement—will be discussed below.

H1: Because EI increases the likelihood of concurrent jurisdiction competition cases, regulatory agents will pursue rule-making cooperation in order to create a formal framework for reducing information asymmetries that could lead to conflicting competition decisions.

H2: Given the higher costs associated with changing non-discretionary authority, competition agents will pursue increases in rule-making cooperation with foreign agents via discretionary means.

H3: Political principals will intervene in agent attempts to shirk (i.e., increase discretionary rule-making cooperation) when the costs of not intervening exceed the costs of intervening.

These hypotheses consider the causal impact of EI and domestic politics on international competition relations. As stated above, EI increases the number of concurrent jurisdiction merger cases. The information available for different competition agents to conduct reviews of such cases is asymmetrical. This information asymmetry increases the likelihood that different competition agents will reach conflicting decisions, which, in turn, increases the likelihood of political intervention in individual cases. Because EI increases the likelihood of conflicting decisions and subsequent political intervention, the behaviour of regulatory agents changes. While the preferences of the agents—maximization of their own certainty and decision making authority—remain stable, they now seek ways to increase information exchanges with their foreign counterparts. Rule-making cooperation (i.e., the creation of a formal framework) is the preferred option for increasing such exchanges. When pursuing rule-making cooperation, agents will opt to shirk because the associated costs are lower than the alternative of getting the principals involved via non-discretionary forms of cooperation like treaty making. However, for their part, the principals are not completely sidelined. Rather, they will still decide to intervene in discretionary rule-making cooperation if the costs of not intervening exceed the costs of intervening. In rule-making cooperation, this intervention occurs via the exercise of control instruments over the domestic competition agents.

The next section tests the above hypotheses with three cases of transatlantic rule-making cooperation. If the hypotheses are supported by empirical evidence, the argument is strengthened that, in an EI environment, increases in agent shirking via discretionary rule-making increase transatlantic cooperation in competition policy. The empirical evidence is drawn from primary and secondary documents, speeches and expert interviews with forty individuals, including EU and US competition officials, business representatives and private-practice competition lawyers. The research was conducted in Brussels, Belgium, and Washington, DC, from 1999-2001.

Each of the hypotheses is tested across three cases of EU-US bilateral competition agreements signed during the 1990s: the Bilateral Agreement, the Positive Comity Agreement and the Administrative Arrangements on Attendance (AAA). H1 relies on a simply binary variable: the presence or absence of agent pursuit of rule-making cooperation. All three cooperative agreements signed during the 1990s and investigated below suggest the presence of agents pursuing rule-making cooperation. Thus, in each case, H2 will be tested on another binary variable: pursuit via discretionary or non-discretionary means. The indicator for this variable is whether the agents launched a specific effort at rule-making cooperation via contacts/institutional avenues under their discretionary authority or via formal avenues for treaty-making. Finally, H3 will be tested on the following binary variable: principals intervene or do not intervene with control instruments. Because each case represents a single event, the exercise of traditional administrative and oversight procedures is an unreliable indicator of principal intervention. Similarly, the non-punitive and extraterritorial control instruments mentioned above are typically exercised as control instruments during individual competition cases. Therefore, a new indicator is required. The indicator for principal intervention is whether or not a

principal attempts to use legal mechanisms grounded in their respective power-sharing agreement to block an agent's attempt to pursue discretionary rule-making cooperation.<sup>21</sup>

## Discretionary Rule-Making Cooperation: three empirical test cases

### The Bilateral Agreement: dispute prevention over dispute resolution

The basic cooperative framework between the EU and US was established through the 1991 Bilateral Competition Agreement. The European Commissioner for Competition, Sir Leon Brittan, launched the initiative for this formal agreement during a speech in February 1990. Taking the 'most likely example,' Brittan warned that due to changing jurisdictional issues, the US and the EU 'may well one day soon take different views of a competition case' (1990: 28). This perception of pending confrontation was reinforced as the Bush Administration began showing signs of more active antitrust enforcement on cases with jurisdictional overlap (Brittan, 1990: 28). Instead of seeking to enhance the Union's capacity for extraterritorial retaliation (e.g., pursuing EU-level blocking and/or clawback statutes), Brittan decided to pursue a new framework for dispute prevention. By preventing international disputes from occurring, competition authorities could preempt intervention by political principals and reduce the likelihood of the reciprocal extraterritoriality that had traditionally characterized dispute resolution in transatlantic competition relations.<sup>22</sup>

Noting the increasing interdependence of the global economy and the EU's coming of age in competition matters, Brittan urged negotiations on dispute prevention with Europe's major trading partners. In particular, Brittan targeted the US:

I personally favour, to start with, a treaty between the European Community and the U.S.A... a party with jurisdiction should be ready not to exercise it in certain defined circumstances, while the other party, in its exercise of jurisdiction, should agree to take full account of the interests and views of its partner. If the parties do exercise jurisdiction concurrently, they should both take account of the interests and views of its partners... [and] take account of each other's concerns and seek to adapt remedies accordingly (1990: 32-33).

Brittan's comments are particularly notable when compared to the substance of the actual agreement that emerged. Also noteworthy is Brittan's desire to begin with a *treaty* on transatlantic competition relations. At the time of the speech, treaties covering competition policy were rare. By 1990, only the US had signed bilateral competition treaties, one each with the Federal Republic of Germany (1976), Australia (1982) and Canada (1984).<sup>23</sup> Brittan was careful to state explicitly that none of these existing treaties 'should be taken as a model' for an EU-US agreement (1990: 31).<sup>24</sup> Rather, the transatlantic relationship required something new.

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21 It is useful to note that the determination of a principal's cost-of-intervention calculations is presently based on post hoc explanations. This current arrangement presents fruitful ground for future research on the factors that contribute to how a principal calculates the costs associated with intervening and not intervening.

22 Prior to 1990, competition agents engaged in limited cooperation under the informal and non-binding framework of the 1979 OECD Recommendation (as amended in 1986). Unlike the OECD regime, a new, formal and binding 'soft' agreement was preferred so that the rules of cooperation would be transparent and unequivocal (Schaub, 1996; cited in Cini and McGowan, 1998: 202). The competition officials pursued a binding act with 'the intention of going beyond the recommendations of the OECD, not only by envisaging more far-reaching forms of cooperation and coordination but also, and above all, by providing for fixed and obligatory forms of conduct in a legally binding act' (ECJ, 1993: 3653).

23 In addition, France and Germany had signed a competition agreement in 1984 (Brittan, 1990: 31).

24 While neither a treaty nor an explicit model, the Commission did acknowledge that the 1986 OECD Recommendation served as 'a frame of reference for the definition of some of the issues relating to the extra-territorial application of the rules of competition which frequently arose between the United States and the EEC' (ECJ, 1993: 3644).

### *Negotiating the 'Soft' Bilateral Agreement*

By the end of 1990, the US had taken up Brittan's suggestion and launched negotiations with the Commission on a possible bilateral competition agreement. However, Brittan's initial desire for a transatlantic treaty on competition relations soon encountered political reality. During the subsequent negotiations, competition officials from both sides of the Atlantic determined that pursuing a (non-discretionary) treaty would impose the excessive costs associated with lengthy and complex domestic approval processes. More specifically, the Department of Justice (DoJ) negotiators resisted pursuing a treaty because the requirement of congressional ratification would be 'too burdensome'.<sup>25</sup> On the EU side, the Commission revised the initial proposal for a treaty after its Legal Service advised the Brittan Cabinet that drafting and signing a treaty would take approximately two years.<sup>26</sup> This timetable was untenable, especially considering Brittan's belief that transatlantic confrontation over competition matters was pending in the very near future.<sup>27</sup> Thus, the competition agents opted to pursue discretionary rule-making cooperation fully cognizant that an attempt at non-discretionary rule-making cooperation via a treaty would have required the undesirable intervention of political principals delaying the process.

The negotiators of the agreement—the agents themselves—decided 'cooperation should occur on the basis of current statutes'.<sup>28</sup> As such, they began crafting a 'soft' agreement that would expand only discretionary cooperation as a means to pursue their statutorily mandated responsibilities.<sup>29</sup> Based on the 1972 Case-Zablocki Act, the US competition agents had clear statutory authority to enter into international executive agreements at their own discretion.<sup>30</sup> It was less clear whether the EU competition officials could exercise similar rule-making authority at their own discretion. Nevertheless, the Commission decided to pursue a binding transatlantic competition agreement via discretionary rule-making cooperation. The decision to proceed was based on a belief that even if the Commission's competence were challenged, it could still present a position that was legally arguable.<sup>31</sup>

With surprising speed, a draft text of the bilateral agreement was negotiated and finalized in July 1991. The Commission forwarded this draft to the national competition officials in each Member States along with an explanatory note that highlighted the need for a 'legally binding document rather than a non-binding recommendation.' This explanatory note was designed to alleviate any potential fears of political principals by suggesting that the draft agreement was an 'administrative' arrangement intended to cover cooperation in discretionary matters. The administrative agreement would enter into force upon signature of the competition agents because it would not require domestic ratification procedures.

As an executive agreement, the bilateral would be legally binding in US law, but would not override domestic law. However, the bilateral was an asymmetrical agreement. While it would be a legally binding administrative agreement in the EU, the bilateral would not bind the Union's courts and political principals. Rather, it would bind the competition agents and be limited to questions falling within their competence (Ham, 1993: 571). The distinct legal classification of the bilateral as

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25 Interview with official in EU's Competition Directorate, February 2001.

26 Interview with former member of Brittan Cabinet, March 2001.

27 In addition, Brittan may have been motivated to finalize an agreement because his tenure as Competition Commissioner was due to expire in approximately two years.

28 Interview with official in EU's Competition Directorate, February 2001.

29 Some commentators label such agreements 'soft' in the sense that 'they are executive agreements that are subordinate to and don't change or override the existing laws of either party' (Stark, 2000: 10).

30 In the US, executive agreements are formal and binding. However, because they have not been ratified by the Senate as treaties, they do not override any inconsistencies in domestic law (ICPAC, 2000: Annex 1-C, v). For more on the role of executive agreements, see Brand (1990) and Margolis (1986).

31 See Commission's legal arguments in *French Republic v. Commission of the European Communities*, Case C-327/91.

an executive agreement in the US and an administrative agreement in the EU reflect the different domestic institutional environments in which the respective competition agents were operating.

In the US, the Bilateral was negotiated under the discretionary authority of the DoJ and Federal Trade Commission (FTC).<sup>32</sup> In the EU, negotiations over the agreement came to a head in September 1991. On September 5, the Commission organized a meeting for national competition officials from the Member States to make comments and observations on the draft bilateral agreement. At this meeting, certain Member States—notably France—raised concerns over the legal basis of and Commission’s competence to sign such a binding international agreement. Member States also raised questions regarding the protection of confidential business information submitted to the Commission and the precise procedures for consultation between the EU and US competition officials. Because of these concerns, the Member States requested that another meeting be held with the Commission after a working group of national experts was convened to discuss the bilateral agreement in more detail.

Sensing a possible derailment of the internal negotiations, Commissioner Brittan ruled that no future meeting would address matters of principle related to the agreement. In particular, Brittan was determined to prevent any discussion over ‘whether it was advisable to conclude a cooperation agreement with the United States in the chosen form’ (ECJ, 1993: 3644). Given the opportunity, the Member States might decide that only the Council of Ministers was competent to sign the transatlantic competition agreement, or worse yet, that a treaty was the more appropriate format for such a bilateral agreement with the US. Brittan did finally agree to convene another meeting on September 9. However, he restricted the agenda to less-contentious technical aspects of the agreement, such as procedures for consultation and protection of confidential information.

Following this meeting and seeking to continue on its momentum, the EU convened the College of the Commission on the next day. At this meeting, minutes indicate that the Commission ‘approved the draft agreement and authorized its vice-president [Brittan] to draw up the final act and to sign and conclude the Agreement itself on behalf of the institution’ (ECJ, 1993: 3645). Acting quickly, the final text was prepared by the US and EU competition officials and signed in Washington, DC, on September 23. As agreed by the competition agents, the Bilateral entered into force upon signature because it did not require ratification in either jurisdiction.

### *Provisions of the Bilateral Agreement*

The actual substance of the Bilateral Agreement addresses most of Brittan’s initial proposals. Generally, the Bilateral Agreement governs formal and informal transatlantic cooperation and has a much more operational and binding character than the previous OECD Recommendations (Devuyst, 2000: 324). The central components of the Agreement include

1. Notification when competition enforcement activities may affect the ‘important interests’ of the other party,
2. Exchange of non-confidential information,
3. Consultation and coordination of enforcement activities, and
4. Conduct of enforcement activities, ‘insofar as possible’, that are consistent with objectives of the other party.

The Bilateral Agreement reduces the potential for EU-US jurisdictional conflict by formalizing exchanges of information. The agreement emphasizes mutual notification by competition authorities during the initial decision-making process in individual competition cases. In merger review, this first step in transatlantic cooperation occurs when one competition authority officially notifies the other that it is reviewing a merger. Acting as an alert system, such notifications are made ‘far enough in

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<sup>32</sup> Per the Case-Zablocki Act, the competition agents also had to acquire legal approval from the US Department of State.

advance... to enable the other Party's views to be taken into account' (Article 2). After the initial notification, further cooperation can take numerous forms in the investigatory and remedial phases of a competition case (Devuyt, 2000: 324).

To allay concerns of political principals, the Bilateral respects US and EU legislation already in force. Specifically, the competition agents agreed that 'Nothing in this Agreement shall be interpreted in a manner inconsistent with the existing [domestic] laws, or as requiring any change in the [domestic] laws' (Article IX). The Bilateral is also flexible enough to allow for the use of extraterritoriality in cases of concurrent jurisdiction, stipulating 'Nothing in this Article... precludes the notifying Party from undertaking enforcement activities with respect to extraterritorial anticompetitive activities' (Article V). In other words, political principals maintain the right to intervene in cases in which they perceive national and/or constituent interests as being threatened.

Possibly the most unique and interesting component of the Bilateral Agreement is the introduction of the principle of comity. This principle of international law relates directly to Keohane's definition of international cooperation because it requires a 'state' to consider the important interests of other 'states' when enforcing domestic laws. Comity can be distinguished as two distinct types: traditional and positive. Moving beyond the OECD's non-binding regime, the 1991 Bilateral Agreement embodied both variants of comity for the first time in a binding agreement relating to competition matters (Ham, 1993: 594; OECD, 1999: 10).

Traditional comity (Article VI) requires a party conducting a merger review to *consider* the 'important interests' of the other party to the agreement.<sup>33</sup> This principle has inspired daily discretionary cooperation between EU and US competition officials. As former EU Competition Commissioner Karel Van Miert acknowledged, 'We are for instance within the realm of traditional comity when we cooperate in a certain case to bring our respective positions and remedies closer to each other in order to avoid creating a harmful effect to the market of the partner' (1998, 2). While the term 'positive comity' cannot be found in the Bilateral Agreement, the legal principle is clearly provided for in Article V. Positive comity differs from traditional comity in that it allows one party to *request* that another party open an investigation into a competition case—located outside the requesting party's jurisdiction—that affects the requesting party's important interests.<sup>34</sup> If an investigation is initiated, the Bilateral requires the requested party to update the requesting party on the investigation and inform them of any relevant decisions taken in the investigation.

### *A Political Challenge to the Bilateral*

Without comprehensive and precise legal boundaries for the authority of the EU's separate institutions, the Commission's competence to sign the Bilateral Agreement was not clear. Nevertheless, the Commission skillfully steered the draft Bilateral Agreement through its uncertain domestic institutional landscape. The Commission was so successful and expeditious that it was able to approve and sign the agreement before significant opposition could be mounted in the Council of Ministers.<sup>35</sup> This success, however, would prove illusory. Shortly after the Commission sent the final text of the Bilateral to the national competition authorities on October 7, complaints began to emerge that the exact procedures for information sharing were unclear and that the Commission had

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33 Traditional comity is also sometimes referred to as 'negative' comity. See ICPAC (2000: 226-240), Kiriazis (1998) for more on traditional comity. On the history of comity, see Ryan (2000), OECD (1999).

34 A legal distinction may also be made between a request that a foreign jurisdiction open or expand an investigation and a request for assistance in a foreign jurisdiction's investigation (OECD, 1999: 3). See also OECD (1999: 5-6) for a further treatment of similar definitional issues of positive comity.

35 The rapid pace at which the agreement was initially drafted and signed not only limited review by and input from political principals in the Council of Ministers, but also limited influence by interest groups, in particular business (Interview with official in Competition Directorate, February 2001).

overstepped its legal authority to enter into agreements with foreign governments—a significant power not readily relinquished by the sovereign EU Member States.

On the other side of the Atlantic, the DoJ and the FTC decided to begin cooperating in accordance with the Bilateral Agreement. The mounting European concerns did not change the US view that the Bilateral was a useful way to facilitate cooperation with the maturing EU. Even if the legality of the agreement was facing a challenge in the EU, the US competition officials still considered it a practical and useful framework for reducing the likelihood of conflicting decisions on cases with concurrent jurisdiction.<sup>36</sup>

The first official challenge to the agreement came from the French Government (supported by the Netherlands and Spain), which formally filed a complaint with the ECJ to annul the Bilateral Agreement. The primary accusation was that the Commission had breached its authority to conclude international agreements, as stipulated in Article 228 of the Treaties of Rome (ECJ 1993, 3646). The legal challenge also reflected frustration over a perceived lack of consultation with the Council of Ministers before the Commission approved and signed the Bilateral Agreement.<sup>37</sup> In 1991, the French also viewed Commissioner Brittan with suspicion as a pro-market Anglo-Saxon who would push for increasingly close cooperation on competition issues and sharing of confidential information with the US. Such an individual was sure to threaten the priorities of French industrial policy.<sup>38</sup>

The French legal challenge delayed the official implementation of the Bilateral Agreement in the EU. With the agreement's future in legal limbo, the Commission still began cooperating with the US competition officials according to the framework and policy implementation procedures established in the Bilateral. On December 16, 1993, the ECJ's Advocate General Tesauro delivered a preliminary opinion supporting the French challenge to the Bilateral Agreement. About eight months later, on August 9, 1994, the ECJ delivered its final judgment. The decision favoured the French argument and ordered the Commission to pay the legal fees associated with the case (ECJ 1994).<sup>39</sup> In effect, the ECJ decision had clarified the EU's principal-agent power-sharing arrangement over rule-making cooperation in all policy areas. The Commission has no discretionary authority to engage independently in rule-making cooperation that results in binding international agreements. However, as long as the Commission engages in *non-binding* rule-making cooperation, it can do so at its own discretion.

### *Re-negotiating the Bilateral*

With the Bilateral Agreement declared void by the ECJ, the Commission began a rapid campaign to acquire the Council's approval of the agreement. On October 12, 1994, the Commission presented a request to the Council for a decision on the Bilateral Agreement.<sup>40</sup> In this communiqué, the Commission made its case for the Bilateral, which is surprising in its candour regarding the need to limit political intervention. The Commission argued that cooperative international agreements were necessary for 'an effective solution to be found to the problems encountered, while at the same time avoiding the conflicts that may arise from a unilateral reaction based on extraterritoriality. It is for this reason that the Commission considers that cooperation agreements must be concluded between competition authorities' (Commission 1994: 2). The communiqué is also noteworthy for the Commission's insistence that the Bilateral would limit US extraterritorial intervention in European

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36 Interview with official in DoJ's Antitrust Division, December 1999.

37 Interview with official in EU's Competition Directorate, February 2001.

38 Interviews with official in EU's Competition Directorate, February 2001; and former member of Brittan's Cabinet, March 2001.

39 For a discussion of the ECJ's judgment on the annulment of the Bilateral, see Riley (1995).

40 In 1995, under the consultation procedure, the European Parliament also approved the Commission's proposal to the Council for the Bilateral (OJ C 043, 20/02/1995 p. 0126).

competition matters because it incorporated ‘a number of principles established by US case-law in order to restrict excesses in the extraterritorial application of US competition rules’ (1994: 2).

The internal Union negotiations resulted in the exchange of a short Interpretive Notice between the EU and US.<sup>41</sup> During this period, the Council of Ministers raised concerns over the protection of confidential information. Much of the Council’s concern, as with businesses, was over the US’s criminal sanctions in cartel cases and the use of confidential information. Put simply, the Council and European business interests did not want European citizens (i.e., businesspeople) to be subject to incarceration in US prisons. Not wanting to challenge domestic legislation, the competition officials succumbed to the institutional constraints by which they were bound to protect confidential information. In particular, the Commission readily acknowledged that it

was bound by the obligations laid down in the Treaty and in the regulations adopted by the Council. This constraint is of particular importance here because of the confidentiality requirement imposed on the Commission under Regulation No. 17 (First Regulation implementing Articles 85 and 86 of the EC Treaty), a requirement from which it could not derogate (1994, 2).

As a result, the Commission presented a ‘Statement on Confidentiality of Information’ to the Council, which guaranteed that only non-confidential information would be exchanged with US competition officials unless businesses waived their rights to confidentiality (European Commission, 1998a: 4-5).

The Commission also issued a ‘Statement on Transparency’ asserting that Member States would be informed when a notification was made to or received from the US competition officials if the resulting cooperation would affect their national interests (European Commission 1996). It was also agreed that the Commission would report annually to the Council and the European Parliament on the implementation of the Bilateral Agreement. As a result, the Council and the Commission promptly issued a Joint Decision on April 10, 1995, officially approving and implementing the agreement.<sup>42</sup>

### *Reasons for Signing the Bilateral Agreement*

The competition agents shared similar incentives for signing the Bilateral Agreement. They desired a formal, binding agreement that would address the new competition challenges raised by the changing EI environment and reduce the likelihood of domestic and international political intervention in competition cases. The structure of information exchanges in the Bilateral is conducive to decreasing the likelihood of conflicting decisions in merger reviews, which decreases the likelihood of political intervention. By providing for the exchange of only non-confidential information, the agreement also prevents principals from getting involved (e.g., changing or creating new domestic law) while still allowing the exchange of enough non-confidential information to reduce the likelihood of conflicting decisions.

The US and EU competition agents also negotiated the Bilateral out of self-interest. For the US, cooperating within the framework of the Bilateral would reduce the likelihood of intervention by European political principals *and* competition agents in concurrent jurisdiction mergers. US competition officials feared the possibility of increased intervention by a ‘maturing’ Union. This maturation was seen in the EU’s new domestic and international control instruments, specifically through three interlinked events: the Wood Pulp doctrine of extraterritoriality, the completion of the single market and the signing of the Merger Control Regulation (Janow, 2000: 30-31).<sup>43</sup>

First, the 1988 Wood Pulp decision was especially important for changing transatlantic relations because it established the extraterritorial jurisdiction of the EU. This decision reinforced the

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41 OJ L 131 of 15.6.95, pp. 38-39.

42 The Commission was included in this Joint Decision because its signature was legally required as the competent authority of the European Coal and Steel Community (Interview with official in Competition Directorate, December 2000).

43 See also James (2001: 4), Stark (2000: 4), Steiger (1995: 4) and Miles (1995: 120).

international reach of any control instruments exercised by the EU. Second, the completion of the EU's single market added further evidence that the Union was maturing. As Stark argues, the single market program 'was in full swing, bringing with it an increase in the powers and visibility of the Commission' (Stark, 2000: 4). The completion of the single market suggested that the EU was becoming a significant international economic actor with more resources for non-punitive control instruments. Third, the EU's expanding role in competition policy was reflected in the 1990 implementation of the Merger Control Regulation (MCR). Not only did the MCR designate the Commission as the lead agency for merger review in the Union, it also created a new Merger Task Force with pre-merger notification authority that could be applied to the behaviour of US firms. The MCR contained specific thresholds above which the Commission would investigate anticompetitive behaviour. Because many US firms engaging in mergers in the EU were large multinational corporations, their activity would almost certainly meet these thresholds. These three factors suggested that the EU's competition agents were increasingly likely to exercise their merger review extraterritorially and impose remedies on US firms even if US competition authorities disagreed.

The EU also had a significant self-interest in negotiating the Bilateral. The Commission negotiated the Bilateral conscious of the various international control instruments available to the US political principals as well as their willingness to use them. By entering into a binding agreement with the US, the EU could create a more balanced transatlantic competition relationship than that which had existed under the non-binding OECD regime (Brittan, 1992: 51). This desire for balance was also directed at the more experienced and historically more active US competition agents' capacity for extraterritoriality.

The EU was also aware of its own rapid maturation in competition policy and conscious that such domestic changes could precipitate conflict in transatlantic competition matters as well as other policy areas (Brittan 1992, 49). Although the EU was maturing, the fact that it was largely untried and lacked significant international control instruments to battle unilateralism (e.g., blocking and clawback statutes) increased the incentive to cooperate administratively with the US competition agents. Of course, the individual EU Member States could still exercise their respective international control instruments against the US, but this was an undesirable recourse to dispute resolution through political intervention. Rather, the Commission needed a method to reduce the likelihood of conflicting decisions without increasing political intervention.

An important but unexpected finding of this case is that competition agents pursue discretionary rule-making cooperation not only to maximize their autonomy from political principals, but also to reduce the likelihood of unilateral extraterritoriality by foreign competition agents. Such actions by foreign competition agents increase uncertainty for domestic competition agents and increase the likelihood of political intervention (i.e., politicization of the case). Thus, cooperation between competition agents is not a simple dynamic of agents versus principals. Rather, EU and US agents appeared fearful of each other's extraterritorial reach at the start of this cooperation.

### **The Positive Comity Agreement: furthering dispute prevention**

Most EU-US cooperation that followed from the Bilateral Agreement developed on the basis of traditional comity and was implemented as daily and discretionary contacts between case handlers. While its proponents on both sides of the Atlantic hailed the Bilateral as a breakthrough, the competition authorities were simultaneously taking steps to clarify positive comity in practice. The first step occurred at a meeting between the EU's Competition Commissioner (Karel Van Miert) and the heads of the DoJ's Antitrust Division (Joseph Klein) and the FTC (Robert Pitofsky) in Washington, DC, on October 16, 1996. Among other issues, the participants discussed the possibility of drafting a new transatlantic competition agreement (European Commission, 1997). Both sides agreed that it would be useful to move forward on a new and separate agreement that would elaborate when positive comity ordinarily would be applied and what specific procedures would be employed

for such a request. The new effort at transatlantic rule-making cooperation resulted in the 1998 Positive Comity Agreement (PCA).

### *Negotiating the PCA*

In the US, work on this new and separate agreement again proceeded along the institutional lines established for rule-making cooperation under the Case-Zablocki Act. These discretionary procedures required negotiation and agreement between the DoJ and FTC. As long as the two competition agents were able to agree on the substance of the agreement, their work did not require political approval. Ultimately, only the Department of State's legal approval was necessary to ensure that the US was not signing a binding international agreement that conflicted with current domestic law. By 1997, the US competition officials moved beyond internal negotiations and began exchanging drafts of the new agreement with their counterparts in the EU.

In the EU, the internal negotiations were more complex. Due to the power-sharing parameters established by the ECJ ruling on the Bilateral, the Commission followed a very different procedure for negotiating the PCA. The Council of Ministers was involved very early, adopting a negotiating brief for the Commission on October 14, 1996, two days prior to the initial meeting in Washington at which the new agreement was to be discussed (Council of Ministers, 1996). Because the intended agreement would be binding on the signatories, the EU political principals remained involved in this case of rule-making cooperation.

On June 18, 1997, the Commission formally adopted and submitted a proposal for the new agreement to the Council. The short proposal notably argued that the new agreement represented a commitment on the part of the US and EU 'to cooperate with respect to antitrust enforcement rather than to seek to apply their antitrust laws extraterritorially' (European Commission, 1997a). The Commission also submitted the agreement to the individual Member States, the European Parliament, industry and other interested parties for opinion (Commission, 1997). Shortly thereafter, the Commission received the Council's approval to enter into the agreement. On June 4, 1998, the Council and the Commission signed the final agreement on behalf of the EU. The DoJ's Antitrust Division and the FTC signed for the US.

### *Provisions of the PCA*

The PCA clarifies the principal of positive comity: 'The competition authorities of a Requesting Party may request the competition authorities of a Requested Party to investigate and, if warranted, to remedy anticompetitive activities in accordance with the Requested Party's competition laws' (Article III). These requests will typically be made when one competition authority is better placed to acquire the necessary information to conduct an investigation. In such a case, the PCA creates the presumption that the competition authorities of a requesting party 'will normally defer or suspend their own enforcement activities in favour of enforcement activities by the competition authorities of the Requested Party' (Article IV). Specific conditions are provided under which a positive comity deferral will be made. For example, deferrals will normally be made when the anticompetitive activities in question do not have a 'direct, substantial and reasonably foreseeable impact on consumers' in the requesting party's territory (Article IV). In other words, if one party feels the anticompetitive behaviour is seriously detrimental to its domestic consumers, that party has the right to conduct a simultaneous investigation of its own.

The PCA procedures increase implementation cooperation by requiring the requested party—'on request or at reasonable intervals'—to inform the requesting party of the status of the investigation. Should the requested party be unable to deal 'actively and expeditiously' with or update the requesting party on a positive comity investigation, the requesting party is free to initiate its own investigation.

Updates of ongoing positive comity investigations must conform to the domestic statutory requirements of the respective parties for protecting confidential information.

### *Avoiding Political Intervention in the PCA*

While negotiating the PCA, EU and US competition officials pursued rule-making cooperation always conscious of the constraints imposed by their respective domestic institutional environments. US competition officials were again able to negotiate an executive agreement with relatively little political intervention. The EU competition officials, having learned their lesson from the ECJ ruling on the Bilateral Agreement, enjoyed comparatively less discretionary rule-making authority but still pursued the agreement as a means to enhance their cooperation with US competition officials.

US and EU competition officials were careful not to insert language into the draft agreement that would require changes to domestic law. Such changes would have necessitated principal intervention as politicians amended and/or drafted new legislation. This approach was unacceptable because it would have increased considerably the costs of negotiating and reduced the likelihood of finalizing the new agreement. To make the point as clear as possible, the competition officials inserted Article VII: 'Nothing in this Agreement shall be interpreted in a manner inconsistent with the existing laws, or as requiring any change in the laws, of the United States of America or the European Communities or of their respective states or Member States.' This provision assured that domestic legal protection for confidential business information would be respected.<sup>44</sup>

Another example of the competition officials' preference to avoid political intervention relates to mergers. The PCA does not cover merger reviews because domestic EU and US merger control laws and pre-merger notification rules take precedence. Specifically, the EU's Merger Control Regulation (MCR) and the US's Hart-Scott-Rodino Act (HSR) preclude the suspension or deferral of domestic merger investigations to foreign competition authorities. Thus, the provisions in the PCA show that the competition agents again consciously decided that cooperation should occur on the basis of current statutes.

### *Reasons for Signing the PCA*

The PCA furthered the creation of a transatlantic framework based on dispute prevention by competition agents instead of dispute resolution by political principals. Similar to the Bilateral, the PCA addresses the new challenges raised by the interaction of the systemic-level EI and competition cases in overlapping jurisdictions. While the applicability of the PCA is limited to non-merger cases, it reduces the likelihood of political intervention and preempts extraterritoriality by competition agents.

The PCA facilitates future implementation cooperation by reducing the likelihood that EU and US competition laws will be applied extraterritorially. In such cases, the competition authorities will normally submit a positive comity request and suspend or defer their own investigation instead of exercising their laws extraterritorially (Van Miert, 1998: 9). This suppression of extraterritoriality reduces the likelihood that political principals will view foreign competition authorities as threats to national and/or constituent interests. In addition, by clarifying the procedures for positive comity requests, the PCA decreases the likelihood of competition agents reaching conflicting decisions (Devuyst, 2001: 136). By reducing the likelihood of conflicting decisions, the PCA also contributes to limiting political intervention.

Both the US and EU competition authorities viewed the PCA as a way to reduce further the likelihood of unilateral extraterritoriality. The desire to reduce the likelihood of extraterritoriality via a

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<sup>44</sup> This protection was extremely important given concerns by competition authorities and businesses that confidential information, once exchanged, could be made public and/or more easily accessed by third parties (e.g., political principals and competitors). Such an occurrence would likely prompt political intervention.

binding agreement becomes particularly evident in the EU position.<sup>45</sup> As Competition Commissioner Karel Van Miert claimed, the issue of extraterritoriality and the imbalance in transatlantic competition relations was again a major factor motivating the EU's desire for this rule-making cooperation:

As the Community has never formally claimed territorial jurisdiction as extensive as that which is claimed by the US, this situation was viewed as an imbalance in our bilateral relations and an obstacle to any further deepening of these relations... We believe that the new draft agreement... will be a significant contribution to rebalancing relations in this respect (1997: 7).

The future application of positive comity should not be exaggerated. Due to the success of the Bilateral Agreement, recourse to the safety-valve of positive comity has been reduced. As Claude Rakovsky, member of EU's Competition Directorate, argues, the Bilateral 'may have been a source of inspiration in daily co-operation,' and this co-operation may have been so good that 'it is not normally necessary to activate formally the (positive or negative) comity procedures' (cited in OECD, 1999: 11). Evidence of the limitations of positive comity can be found in the fact that, to date, there has been only one formal request for an investigation under the PCA: the Sabre/Amadeus case.<sup>46</sup>

The signing of the PCA shows that the competition officials were so eager to clarify procedures of positive comity that they went ahead with binding rule-making cooperation (including the EU working within its more restrictive and higher-cost institutional framework) even though the resulting agreement promised little in the way of increasing further discretion. For example, the principle of positive comity is not frequently used and the PCA does not even apply to mergers, the area in which most transatlantic competition relations occur. This limitation is a direct result of the competition officials' preference to avoid political intervention by not pressing for changes in domestic competition laws on merger control. Thus, the signing of the PCA reflects the concern of competition agents to reduce foreign and domestic political intervention while simultaneously preempting extraterritoriality by their fellow competition agents.

### **Administrative Arrangements on Attendance: non-binding dispute prevention**

In addition to the binding Bilateral Agreement and the PCA, the EU and US competition authorities have also engaged in non-binding, rule-making cooperation. On March 31, 1999, the EU and US competition authorities signed the Administrative Arrangements on Attendance (AAA).<sup>47</sup> This formal agreement was designed to enhance implementation cooperation in competition cases. As such, it formalizes procedures for competition authorities to attend (on a reciprocal basis) hearings held during each other's merger review process. Because the AAA is non-binding, both competition authorities were able to negotiate the agreement entirely at their own discretion.

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45 The EU was also concerned at recent developments in US extraterritoriality. See, for example, the 1993 judgment of the US Supreme Court in *Hartford Fire Insurance Co. v. California*, 113 S.Ct. 2909. It has been argued that this decision 'dealt comity a near death blow... by limiting comity considerations in most situations to those conflicts where one sovereign has compelled the very conduct which the other sovereign forbids' (Waller, 2000: 564). An additional factor that may have increased the likelihood of US extraterritoriality and contributed to the EU's position concerned the infamous footnote 159 in the DoJ and FTC's *Antitrust Enforcement Guidelines for International Operations* (April 1995), reprinted in 4 Trade Reg. Rpt. (CCH) 13,107. During the period between the 1991 Bilateral Agreement and the PCA, the US DoJ removed footnote 159 from their international guidelines, which was viewed as an indication that the US planned to undertake enforcement actions against activities restraining US export commerce. For more on this footnote, see Janow (2000: 31-32) and Varney (1996: 18).

46 For discussions of Sabre/Amadeus, see Janow (2000, 39-40) and Devuyt (2001, 140-42). While only one formal notification under has occurred PCA, Janow notes three other informal notifications that resemble the principle of positive comity: AC Nielsen, Parma Ham, and Marathon Oil (2000: 38-39).

47 See Bulletin EU 3-1999, Competition (18/43).

### *Origins of the AAA*

When conducting their respective merger reviews, competition authorities frequently meet with the merging firms and third parties as a way to increase their information on the likely impact of the merger.<sup>48</sup> These meetings are known as ‘oral hearings’ in the EU and ‘pitch meetings’ in the US. As provided for in the EU’s MCR, oral hearings are held by the Merger Task Force and conducted by an independent Hearing Officer. In the US, the DoJ’s Antitrust Division and the FTC hold their own respective pitch meetings. The AAA allows representatives of foreign competition authorities to attend these discretionary meetings in cases of mutual interest (i.e., concurrent jurisdiction mergers).

In 1997, prior to negotiating the AAA, the US DoJ and FTC formulated requests to attend oral hearings being conducted by the EU’s Competition Directorate (European Commission, 1998a: 12). After reviewing these requests, the Directorate (specifically, the Hearing Officer) invited officials from the US competition authorities to take part as observers in the oral hearings. These invitations were specific to reviews being conducted for three separate merger cases: Boeing/McDonnell Douglas, Guinness/Grand Metropolitan and WorldCom/MCI (Devuyst, 2001: 136). Because the US officials attended the hearings as observers, they were not authorized to participate or intervene in the proceedings.

The Commission’s decision to accept the US’s requests for attendance ‘took into account that the US authorities were examining the same transactions and that attendance in the hearings could improve cooperation and coordination of enforcement activities’ (Devuyst, 2001: 136). Based on this experience, the EU believed that further attendance at foreign hearings could prove very beneficial to the analysis of concurrent jurisdiction mergers (i.e., reduce the likelihood of conflicting decisions). As a result, the Commission ‘proposed an exchange of letters’ with the US competition authorities in order ‘to establish a clear framework for such requests and to ensure their reciprocal nature’ (Devuyst, 2001: 136).

### *Negotiating the AAA*

Not surprisingly, the US competition officials were able to negotiate these new administrative arrangements entirely at their own discretion. Careful to highlight its discretionary authority to sign the formal AAA, the Commission noted that ‘Neither these administrative arrangements, nor the letters exchanged between the Commission and the US competition authorities, outlining and confirming a common understanding of the said arrangements, constitute a binding international agreement’ (European Commission 2000a: 5). Because the AAA would not be binding, the Commission was not constrained by the ECJ’s 1995 decision on the Bilateral Agreement. Thus, the EU Competition Directorate was able for the first time to pursue discretionary rule-making cooperation unabated by the Council. In addition, because the agreement was simply a non-binding administrative arrangement, the Directorate for External Affairs was not closely involved either.<sup>49</sup>

### *The AAA in Practice*

Based on the AAA, reciprocal exchanges of attendees have now become frequent occurrences in merger cases of concurrent jurisdiction. Before the AAA, requests for attendance were dealt with on a case-by-case basis. Now, the procedure to gain attendance has been regularized. As the EU’s Competition Commissioner Mario Monti argues ‘it has now become standard practice for representatives of the antitrust agencies to attend oral hearings in cases involving close EU-US cooperation—a virtually unprecedented step forward in EU-US regulatory cooperation’ (2001a: 3). By simplifying the procedure for attendance into a standard practice, cooperation has been enhanced, which, at least marginally, reduces the likelihood that competition agents will reach conflicting decisions.

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48 The AAA also applies to non-merger cases.

49 Interview with official in EU’s Directorate for External Affairs, May 2001.

Exactly who will be allowed to attend these hearings is determined exclusively at the discretion of the competition authorities.<sup>50</sup> The DoS is not involved on the US side, and neither is the Council, Directorate for External Affairs or the individual Member States on the EU side. Before an arrangement for attendance is completed, the host competition authorities will typically consult with the merging firms. When requests for attendance are granted, the prevailing laws protecting confidential information in the host jurisdiction apply to the guest authorities. Unless the merging firms have agreed to waive their right to confidentiality, guest competition authorities are asked to exit the meeting when confidential information is being discussed. As such, the AAA does not threaten domestic laws on confidential information. It is possible that a request for attendance can be denied. The AAA mentions that attendance will be granted for 'appropriate' cases. Thus, a competition authority can 'decline to invite attendance by the requesting competition authority, if it believes that the other's attendance would adversely affect the proceedings or would otherwise be inconsistent with important interests' (Devuyt, 2001: 137).

The AAA further decreases the likelihood that competition agents investigating concurrent jurisdiction mergers will reach conflicting decisions because it reduces the information asymmetries between the agents. However, reciprocal attendance does not guarantee consistent decisions. The BOC/Air Liquide merger in December 1999 was one such case. Following a request by the FTC to attend the EU oral hearing, this merger represented the first time the AAA was formally invoked. While the FTC attended the hearing, the competition authorities ultimately ended up in 'disagreement' over the merger case (Commission, 2000a: 5-6). Thus, the AAA is not able to change the underlying domestic laws upon which the two respective competition authorities analyze mergers. Indeed, the competition officials are unlikely to request such changes to domestic laws.

While the AAA has its limits, the agreement does contribute to successful transatlantic cooperation in the implementation of competition policy. By reducing the likelihood of conflicting decisions, the AAA (like the Bilateral and PCA) reduces the likelihood of political intervention via international and domestic control instruments. The exchange of attendees and, thus, information also preempts the extraterritorial imposition of conflicting remedies by foreign competition agents.

## **Conclusions**

Transatlantic competition relations have witnessed an unexpected transition from dispute resolution by political principals to dispute prevention by regulatory agents. This transition was a response to the challenges of EI and has occurred through largely discretionary processes that reflect the similar preferences of regulatory agents operating in different domestic institutional environments. Without competition agents pursuing their preferences to maximize certainty and decision making authority, political principals likely would have responded to the new challenges of EI and the increasing likelihood of conflicting decisions by creating new international instruments to control foreign regulatory agents or by entering into non-discretionary rule-making cooperation via treaties. Neither of these outcomes occurred. Rather, the competition agents pursued rule-making cooperation via discretionary means in order to create a framework for reducing the information asymmetries that could lead to conflicting decisions.

The preceding analysis provides substantial evidence supporting the three hypotheses discussed above. While the US competition agents enjoyed comparatively more discretionary authority to engage in rule-making cooperation, the European Commission was able to overcome domestic constraints on its rule-making authority. The case of the Bilateral Agreement clearly shows the constraints faced by the EU. The French decided to intervene in this case because the costs of not intervening (essentially granting the Commission discretionary authority in rule-making cooperation)

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50 In the EU, this decision is made by the Hearing Officer.

were too high. While negotiating subsequent agreements with the US, the Commission overcame this political resistance by conforming to the power-sharing arrangements established after the ECJ's 1995 decision. Overcoming the different domestic institutional environments, US and EU regulators were able to increase cooperation as a means to decrease the likelihood of conflicting decisions and political intervention. By decreasing the likelihood of conflicting decisions and political intervention, the competition agents pursued their preference for maximizing their own certainty and decision making authority in subsequent policy implementation. The political principals also pursued their preference for intervening with control instruments when the perceived costs of agent shirking in rule-making cooperation exceeded the costs of not intervening.

The Commission's willingness to pursue international cooperation in its more costly domestic rule-making environment (especially while negotiating the PCA) may reflect the comparatively early stage of its institutional development in competition policy. While the US already enjoys a full arsenal of extraterritorial and countermeasures, the EU consciously and consistently resisted expanding the Union's institutional capacity for extraterritorial retaliation (e.g., pursuing EU-level blocking and/or clawback statutes). The EU may have been more willing to pay the higher costs associated with its domestic rule-making environment because it saw international cooperation as a way of enhancing its credibility in competition policy. Compared to the US competition agents, the Commission was likely more concerned with increasing credibility because it is a maturing, administrative-regulatory agent.

Throughout the three cases investigated, it becomes apparent that the EU and US competition agents carefully avoided cooperating in ways that would require changes to domestic legislation. Because the Bilateral Agreement is not a treaty, it does not change existing domestic law. While the Bilateral explicitly allows for extraterritoriality, more importantly, it reduces the likelihood of such unilateral behaviour by increasing discretionary implementation cooperation between agents through notification, exchange of information, coordination of remedies and new measures like comity. This cooperation does not eliminate the possibility of conflicting views, but it does reduce the risks of divergent decisions.

The Positive Comity Agreement and AAA also further clarified and increased discretionary forms of transatlantic implementation cooperation. Both agreements were negotiated by the US competition agents via their discretionary rule-making authority. Because the PCA is a binding agreement, the EU lacked equivalent discretionary rule-making authority. As a result of the lessons learned from the ECJ's 1995 decision on the Bilateral Agreement, the Commission conformed to its new, non-discretionary rule-making procedures while negotiating the PCA. Seeking to enhance cooperation further, US and EU competition agents were able to negotiate the non-binding AAA solely under their discretionary rule-making authority. Both agreements carefully avoided mandating changes to domestic legislation: the PCA respects confidentiality of information and does not apply to merger review, and the AAA also protects confidentiality of information.

Competition agents clearly prefer avoiding both domestic and foreign political intervention. However, an unexpected and important finding is that the agents also prefer avoiding extraterritorial intervention by foreign competition agents, such as the imposition of inconsistent or conflicting remedies in cases of mutual interest. In order to reduce the likelihood of extraterritorial agent intervention, the agreements encourage 'balance' in transatlantic competition relations. The reason for this appears simple: domestic political principals perceive extraterritoriality by foreign agents as a threat, which increases the likelihood of political intervention. Thus, the agreements reduce the likelihood of extraterritoriality by agents, which, in turn, reduces the likelihood of political intervention. This finding suggests that, when applied to international regulatory cooperation, the principal-agent insights of PAM must be expanded to include agent-agent dynamics.

The current study has focused on the initial creation of a formal framework for transatlantic competition relations. However, further research and hypothesis testing is required to understand the dynamics of implementing this cooperative bilateral framework. Like rule-making cooperation, it

appears that subsequent processes of cooperation in transatlantic competition relations are also largely discretionary in nature. This cooperation raises several interesting questions regarding the possibility of substantive and procedural convergence in US and EU competition policy. Careful comparisons with EU-US cooperation in other policy areas are also necessary to determine whether cooperation in competition relations can actually serve as a model for transatlantic cooperation more generally.

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