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Reza Rajabiun, *York University*

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Reza Rajabiun*

*York University, rezarajabiun@osgoode.yorku.ca

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Abstract

The relationship between the design of competition laws and economic outcomes remains the subject of considerable controversy in both law and economics. Recent cross-national studies suggest that effective legal constraints against anticompetitive practices can enhance prospects for economic development by increasing the number of market participants and the quality of broader political and economic institutions. This paper explores the linkages between regulatory constraints against anticompetitive practices and the efficiency of market mechanisms by focusing on the experience in Poland between the collapse of central planning and regulatory harmonization pursuant to European Union accession. The analysis suggests that per se prohibitions and a narrow bureaucratic mandate provided relatively credible and predictable constraints against anticompetitive agreements and practices during the formative days of the market system in Poland. The evidence has implications for other jurisdictions that instead implement the rule-of-reason approach to the design of competition law during the 1980s and 1990s.

KEYWORDS: competition law, per se prohibitions, rule-of-reason, development economics

I. INTRODUCTION

Following the collapse of socialism and central planning in the late 1980s, the subsequent decade was marked by sweeping political and economic liberalization policies across the globe. Although these policies have been successful in promoting economic development in some jurisdictions, they have not provided a basis for poverty reduction or sustained growth in others. The observed divergence of development outcomes following the implementation of broadly similar trade and financial policies represents an important empirical puzzle in the study of comparative development and policy analysis.

As part of the broader economic policy reform measures, lawmakers in many jurisdictions also adopted statutes prohibiting anticompetitive agreements and abusive practices.[1] Nevertheless, the limited capacity of this first generation of competition laws to enhance the institutional capacity for development stimulated some policy debates by economists and legal scholars as early as the late 1990s.[2] A number of recent empirical studies have tried to establish whether there is a link between legal constraints against anticompetitive practices and economic outcomes. This paper analyzes the role of competition law in the development of a market economy in Poland following the collapse of central planning.

As in many other post-socialist jurisdictions, employment and production contracted severely in Poland in the late 1980s and early 1990s.[3] However, the Polish economy adjusted relatively rapidly to the shocks starting a period of aggregate growth and increased prosperity.[4] Per capita income grew at an average annual rate of about 5% between 1990 and 2003 in Poland.[5] In contrast, per capita income in the Russian Federation for example contracted by around 2% annually over the same period.[6] The divergent paths of economic growth are plausibly a product of a wide range of social, economic, and political factors. This analysis

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[1] M. Palim, *The Worldwide Growth of Competition Law: An Empirical Analysis*, 43 Antitrust Bulletin 1 (1998), 105.

[2] J. Tirole, *The Institutional Infrastructure for Competition Policy*, Paper presented at the roundtable on New Comparative Economic Systems, World Bank (1999); S. Evenett, *Links between Development and Competition Law in Developing Countries*, Report to UK Department of International Development (2003); and J. Preston, *Competition Policy and Economic Development: Some Country Experiences*, U.K. Department for International Development (2003).

[3] B. Milanovic, *Poverty in Poland, 1978-88*, 38 Review of Income and Wealth 3 (1992), 329-340. World Bank World Development Indicators (WDI) 2007.

[4] For an overview policy developments prior to EU accession see: *National Report on Structural Reforms on the Products and Services Market and on Capital Markets*, Government of Poland (2003).

[5] WDI.

[6] *Ibid*.

hypothesizes that the design of competition regulations was one of the factors that distinguished the transition process in Poland from the experience of other countries that implemented broadly similar economic policies under relatively similar conditions. The evidence from Poland highlights a number of important policy lessons relevant to jurisdictions contemplating reforms to the competition statutes they first adopted in the 1980s and 1990s.

The next section reviews recent studies on the relationship between laws against anticompetitive practices and economic outcomes, describes the main design features of existing regimes, and explains the relevance of this study in the context of the literature. Section III characterizes the economic conditions and political factors that conditioned the adoption and implementation of a relatively effective competition regime in Poland in the 1990s. Section IV reviews the design of substantive prohibitions and enforcement institutions prior to the harmonization of Polish laws with European Union accession requirements. Section V employs firm level surveys to describe the impact of competition regulations on the level of market power by incumbent enterprises and perceptions of the costs of anticompetitive practices. The final section draws inferences from the Polish experience for the design of competition law as an instrument of development policy.[7]

II. COMPETITION LAW DESIGN AND EFFECTIVENESS IN A COMPARATIVE CONTEXT

Kee and Hoekman (2007) have conducted a large-scale empirical analysis of the effect of the adoption of competition laws across 28 industries in 42 industrialized and developing countries over a period of almost 18 years.[8] Their analysis aims to address one of the fundamental challenges in the assessment of legal constraints on anticompetitive practices. The new competition laws were generally enacted during a period of liberalization in external trade regulations, macroeconomic instability, and fiscal crises. Consequently, directly measuring and comparing the

[7] Background and legal material used here are drawn from a wide range of governmental sources including: Polish Office of Competition and Consumer Protection (OCCP); Organization for Economic Cooperation and Development (OECD), Reports and communications with Polish competition authorities; and European Commission (EC), Material on the legal systems of member states. Where relevant, the meaning of legal material has been checked across different translations and agencies that provide information on enforcement activities. Summary economic data are drawn from the World Bank World Development Indicators (WDI), Polish Ministry of Finance, and Ministry of Economy and Labor. Survey data is drawn from the World Bank Productivity and Investment Climate Surveys (PICS) database.

[8] H. L. Kee, and B. Hoekman, *Imports, Entry and Competition Law as Market Disciplines*, 51 European Economic Review 4 (2007), 831-858.

relationship between the laws and indicators of market competition across diverse jurisdictions requires robust controls for variables such as changes in external trade regulations.

The analysis by Kee and Hoekman (2007) attempts to isolate the effect of the adoption of new competition laws on the level of industry mark-ups from the effect of other factors including the degree of openness to international trade.[9] Traditional price theory views competition law as an exercise in controlling practices that drive up prices and allow some firms to capture super-normal profits. The evidence provided by Kee and Hoekman (2007) suggests that when controlling for import penetration, simply enacting a competition law does not lower the sustainable margins of incumbent suppliers. In other words, the findings provide little support for either private interest theories of regulation that suggest competition law functions to protect inefficient incumbent concentrations, or public interest theories according to which the law constrains the costs imposed by coalitions of cartels/oligarchs on the rest of the economy.[10]

However, the evidence also suggests that enacting a competition statute indirectly lowers the price-setting powers of incumbent firms in the longer run. Specifically, Kee and Hoekman (2007) find that the adoption of a competition law had a significant positive effect on the number of firms in a particular industry, which indirectly reduced the mark-up levels over time.[11] They do not explore the specific channels through which the laws influenced the number of participants.

The new competition regimes are typically a complex set of standards for regulating anticompetitive practices, and summarizing them in a manner useful for cross-country analysis is difficult. Kee and Hoekman (2007) simply use a dummy indicator for competition law adoption. This approach is admittedly rudimentary, and does not shed light on which substantive and procedural features of the laws are more or less likely to be successful as credible constraints against anticompetitive practices or act to enhance the contestability of market institutions.

To develop a richer empirical picture of existing legal regimes, Voigt (2006 and 2008) conducted a survey of competition authorities in a large number of countries.[12] He reported that by 2006, around 90 national jurisdictions had some laws on the books aiming to protect or promote competition. Using the surveys he

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[9] *Ibid*.
[10] J. Buchanan and D. Lee, *Private Interest Support for Efficiency Enhancing Antitrust Policies*, 30 Economic Inquiry 2 (1992), 218-224.
[11] In particular see Section 5, Table 6.
[12] S. Voigt, *The Effects of Competition Policy on Development: Cross-Country Evidence Using Four New Indicators*, Journal of Development Studies (forthcoming 2008) and S. Voigt, *Competition Policies Matter – At Least at the Margin: Cross-Country Evidence Using Four New Indicators,* Paper Presented at the Canadian Law and Economics Association Conference, Toronto (2006).

compiled four indices of substantive and procedural features of the laws and studied the association between these indicators and long-term aggregate total factor productivity (TFP) growth. The growth regression methodology suggests a small positive association between competition law indicators and productivity growth. However, when controlling for general institutional quality, this effect dominates and the results with respect to competition laws disappear.

According to the above outlined studies, lawmakers in most jurisdictions appear to have designed prohibitions against anticompetitive agreements and abusive practices as a complex set of standards typically referred to as the rule-of-reason approach. Evidence of this approach to regulatory design can be found in the objectives of the laws. In addition to protecting or promoting competition, many of the laws incorporate a number of other objectives. The surveys by Voigt (2006) show that besides competition, the average jurisdiction has 3.5 additional objectives on the books. Common secondary objectives include furthering technological progress, improving international competitiveness, and regional development concerns.[13]

The multiplicity of objectives suggests that the new competition laws aim to function as instruments for balancing potentially inconsistent social and economic policies. The presence of an efficiencies defense, which also requires a case-by-case assessment of gains from particular restrictions on competition, is also a common feature of the new regimes. The rule-of-reason approach to legal design aims to ensure that the law is not used to discourage competition or prohibit behavior lessening competition in circumstances where the overall effect of the behavior would be to enhance social and economic welfare. The prevalence of the rule-of-reason approach to the design of substantive prohibitions in the contemporary national competition regimes motivates this study.

In addition to the homogeneity in substantive design of the new competition regimes introduced in the 1980s and 1980s, most jurisdictions also delegate exclusive enforcement authority to a public competition bureaucracy. High powered *per se* prohibitions and private rights of action are indeed rare in the comparative context. This implies that in terms of the overall design of competition laws, developing countries appear to have followed the example of post-World War II Western Europe and Japan rather than the model provided by the Sherman Antitrust tradition in the United States.[14]

The widespread replication of the rule-of-reason approach potentially reflects the fundamental disadvantage of implementing competition law as a set of

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[13] *Ibid*.

[14] See: D. Gerber, *Law and Competition in Twentieth Century Europe* (Oxford University Press, 1998); J. Roberts, *International Comparative Analysis of Private Rights of Access,* Industry Canada, Competition Bureau (2000); and D. Ginsburg, *Comparing Antitrust Enforcement in the United States and Europe,* 1 Journal of Competition Law and Economics (2005), 427-439.

per se prohibitions against collusive agreements, vertical restrictions, or abusive practices by dominant enterprises. The New Institutional Economics (NIE) literature has long pointed out that public enforcement of excessively rigid competition rules limits the range of organizational forms available for private contracting. Specifically, Williamson (1983) argues that relative to the common law tradition in the interpretation of contracts, antitrust law has often been inhospitable to unorthodox organizational forms for production and exchange.[15] A similar sentiment is reflected in the justification expressed by Singh (2002) for the implementation of a case-specific approach to the design of competition law in developing and transition countries.[16] He argues that competition laws that aim to enhance prospects for development should try to optimize competition and coordination incentives of different industries based on their particular needs, rather than trying to maximize the degree of competition. This perspective suggests that the rule-of-reason has advantages to *per se* prohibitions because it allows public enforcers to exempt practices or transactions that increase social and economic welfare, minimizing expected false positive errors.

However, the literature on the economics of substantive design highlights that the implementation of public laws through standards is more information intensive than bright line rules.[17] Christensen and Kerber (2006) observe a trend towards broader application of a "more economic approach" in competition policy in the United States and European Union.[18] They review the literature on the economics of substantive design and point out that *per se* rules tend to:

- Stabilize market expectations relative to a case-by-case approach, since firms can more easily predict what practices are legal/illegal.
- Limit rent seeking behavior by constraining the discretion inherent in the economic approach to designing and interpreting prohibitions.
- Reduce information requirements of regulation.

The theoretical advantages and limitations of *per se* and the rule-of-reason design strategies imply that lawmakers face a serious dilemma in designing substantive features of a competition regime:

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[15] O. Williamson, *Credible Commitments: Using Hostages to Support Exchange*, 73 American Economic Review 4 (1983), 519-540.

[16] A. Singh, *Competition and Competition Policy in Emerging Markets: International and Development Dimensions*. G-24 Discussion Paper Series, No. 18. United Nations (2002).

[17] For an analysis of the generic trade-offs between *per se*/bright line rules versus standards see D. Friedman, *Law's Order: What Economics Has to Do with Law and Why it Matters*, (Princeton University Press, 2000).

[18] A. Christansen and W. Kerber, *Competition Policy with Optimally Differentiated Rules Instead of "Per se Rules vs. Rule of Reason"*, 2 Journal of Competition Law and Economics (2006), 215-244.

- *Per se* prohibitions or the legal approach to regulatory design:
  Restrictive and predictable *per se* prohibitions can lower the probability of undesirable transactions, or false negatives, but increase the likelihood of preventing those that are socially desirable.
- The rule-of-reason or economic approach to regulatory design:
  Standards provide competition authorities or judges with a large degree of discretion to balance competing interests. This might limit the propensity of competition law to be used to discourage or prevent conduct that would enhance welfare. This may not be the case in practice however since discretionary standards also open the door for powerful economic entities to employ competition law as an instrument for subverting market competition.

Although many jurisdictions rely exclusively on the rule-of-reason approach to substantive design, others have solved this dilemma by differentiating between the types of rules they institute to constrain different classes of anticompetitive practices. For example, some jurisdictions prohibit horizontal price fixing and vertical restraint using *per se* prohibitions, but apply a rule-of-reason standard to the treatment of abusive practices.[19] Given the presence of such tradeoffs, the aversion to *per se* prohibitions on price fixing and bid rigging, interlocking directorate structures, and abusive practices by dominant enterprises in the competition regimes introduced in the 1980s and 1990s is puzzling.

This suggests the relevance of other factors than the false positive problem in explaining the design of legal systems aiming to constrain anticompetitive practices.[20] Palim (1998) provided an empirical analysis of economic and political conditions leading to the growth of competition law and found that enactment of the statutes typically coincided with large scale economic crises. Adopted as part of broader trade and financial policy reforms, Maher (2002) emphasized the role

[19] The tension between the two design strategies is also of relevance in the EU integration process and remains controversial in the United States, a jurisdictions which has relied primarily on *per se* prohibitions and private enforcement of legal constraints on anticompetitive practices. For instance, in 2007 the U.S. Supreme Court overruled the nearly century-old precedent established in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911) prohibiting resale price maintenance on a *per se* basis. In *Leegin Creative Leather Products, Inc. v. PSKS, Inc. No. 06-480, 551 U.S.(June 28, 2007)* the court declared that minimum price agreements may benefit consumers, and hence should be subject to case-by-case analysis.

[20] For an analysis of the capacity of legal transplants see: D. Berkowitz, K. Pistor, and J.F. Richard, *Economic Development, Legality, and the Transplant Effect*, 47 European Economic Review 1 (2003), 165-195.

of international organizations and conditionality in shaping and drafting of the national regulations.[21] The circumstances help explain the homogeneity of the new regimes in terms substantive and procedural design.

The experience with the implementation of competition law in emerging market systems in Central and Eastern Europe provides an interesting basis for the analysis of questions raised about the design of legal constraints against anticompetitive practices. Varady (1999) studied the legislative basis and administrative practice in a number of post-socialist jurisdictions.[22] His analysis reveals some degree of heterogeneity in the design and practice of competition law between Central and East European countries. Specifically, jurisdictions in the Former Soviet Union appear implemented a more flexible rule-of-reason approach than those in Central Europe.

In terms of practice in the early stages of transition Varady (1999, p. 259) also points out that competition bureaucracies in Former Soviet states often emphasized the enforcement of rules against unfair competition over prohibitions against anticompetitive agreements and abusive practices. He argued that the competition laws introduced "made little effort to respond to the peculiar economic heritage of particular countries; they were essentially not designed the way one would devise transitional rules for a period of transition."[23] Kovacic (2002) reviewed the mixed experience of former socialist countries in Central and Eastern Europe with competition law during the 1990s, and attributes failures to the high degree of complexity of standards in some jurisdictions.[24]

Dutz and Vagliasindi (2000) provided an empirical assessment of the implementation of competition policy and law in transitional Central and Eastern Europe of the mid to late 1990s.[25] They defined a range of implementation criteria and quantified aggregate measures of competition law and the competitive environment for 22 post- socialist jurisdictions. The three general dimensions of competition regulation they constructed serve as the point of departure for the analysis of links between the design of competition law and market outcomes provided in this paper. They defined the effectiveness of competition law in terms of:

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[21] I. Maher, *Competition Law in the International Domain: Networks as a New Form of Governance*, 29 Journal of Law and Society 1 (2002), 112-136.

[22] T. Varady, *The Emergence of Competition Law in (Former) Socialist Countries*, 47 The American Journal of Comparative Law 2 (1999), 229-275.

[23] *Ibid*, p. 272.

[24] W. Kovacic, *Institutional Foundations for Economic Legal Reform in Transition Economies: The Case of Competition Policy and Antitrust Enforcement*, Chicago-Kent Law Review 77 (2002), 265.

[25] M. Dutz, and M. Vagliasindi, *Competition Policy Implementation in Transition Economies, An Empirical Assessment*, 44 European Economic Review 4-6 (2000), 762-772.

- Enforcement effectiveness: An index of the ratio of sanctions imposed to reported violations, accounting for fines against horizontal cartels and enforcement against anticompetitive acts by executive government bodies.
- Competition Advocacy: Involves an assessment of the effectiveness of written comments and objections concerning other policies and judicial decisions relating to privatization and the regulation of infrastructure. Furthermore, this component includes educational and consumer advocacy roles played by the bureaucracy.
- Institutional effectiveness: Reflects an appraisal of the degree of political independence of the competition authorities, the effectiveness of the appeals process against the bureaucracy, and the transparency of the agency.

To capture the impact of these indicators on economy-wide intensity of competition, Dutz and Vagliasindi (2000) further construct an aggregate enterprise mobility indicator from firm level surveys.[26] Their enterprise mobility indicator captures the frequency, or ease, with which new private enterprises in the region were able to expand employment while also increasing productivity. They found a robust positive correlation between the overall indicator of effectiveness of competition law and the intensity of market competition as measured by the enterprise mobility indicator. Moreover, enforcement level and institutional effectiveness explained most of the statistical association between the variables, while advocacy had limited impact.

Their study reveals that some post-socialist jurisdictions managed to develop effective systems of competition law in a relatively short period, but others did not. According to the Dutz and Vagliasindi (2000, p. 767) indicator, some jurisdictions managed to build competition law mechanisms that were twice as effective by 1997 as those in other countries.[27] A divergence of this magnitude is present in the case of Poland and Russia, for instance. The Polish experience provides a unique basis for learning about the co-evolution of legal and economic institutions that condition how competition laws can function as instruments of development policy.

III. ECONOMIC AND POLITICAL DRIVERS OF COMPETITION LAW

The literature on divergent paths of transition provides a number of possible explanations for the specific features of regulatory institutions that conditioned

[26] *Ibid*.
[27] *Ibid*. p 767.

the evolution of the economy. Economists typically emphasize the importance of the privatization process and the initial allocation of property rights in explaining longer term economic outcomes. Parente and Rios-Rull (2005) for example argued that the key impediment to economic growth that explains cross-national income differences relates to the acquisition of monopoly rights by production input suppliers.[28] The analysis in this paper explores how competition laws helped constrain the abusive practices by enterprises that emerged from the privatization process in Poland.

A second body of studies emphasizes the importance of specific patterns of intra-class conflict and cooperation in policy choices at the early stages of transition in explaining long term development outcomes. King (2002) for instance explains the divergence in terms of the composition of coalitions that gained political and economic power in Poland and the Former Soviet Union.[29] In Poland, a coalition of labor unions and anticommunist intellectuals achieved political control, breaking linkages between socialist and emerging capitalist elites. Despite a change in economic and political ideologies in the Former Soviet Union, socialist elites retained control of both industry and government. This perspective helps explain differences in the design of regulatory regimes aiming to constrain anticompetitive practices in the early 1990s.[30] Existing studies suggest that the legacy of socialism and the political environment were important factors in shaping the relationship between the state and markets that emerged during the 1990s.

A. Historical Legacy and the Transition Path

The approach to the organization of economic policy and planning that evolved in Poland after World War II (WWII) represented a relatively successful example of central planning. Influential economic theorist and diplomat Lange (1949) argued that political decisions in Poland shaped the objectives of the plan to promote industrialization, and eliminate surplus labor in the agricultural sector.[31] However, he argued that this or other macroeconomic policy preferences of a socialist state did not eliminate the necessity of microeconomic choices about which goods to

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[28] S. Parente and J. Rios-Rull, *The Success and Failure of Reforms in Transition Economies*, 37 Journal of Money, Credit, and Banking 1 (2005), 23-42.

[29] L. King, *Post Communist Divergence: A Comparative Analysis of the Transition to Capitalism in Poland and Russia*, 37 Studies in Comparative International Development 3 (2002), 3-34.

[30] For an empirical analysis of linkages between economic and political institutions during the transition see: B. Slantchev, *The Political Economy of Simultaneous Transitions: An Empirical Test of Two Models*, 58 Political Research Quarterly 2 (2005), 279-294.

[31] O. Lange, *The Practice of Economic Planning and the Optimum Allocation of Resources*, 17 Econometrica (1949).

produce and in what quantities.[32] Despite the difficulties in figuring out these variables through central administration, socialist economic planning in Poland resulted in rapid reconstruction from the ravages of the war, and sustained for decades to come.

According to Lange, initial economic success had two central reasons. First, the planned economy was able to achieve full employment relative to decentralized alternatives at the time, even if some idle labor persisted in rural areas. Second, the planned economy and public ownership eliminated the restrictions to the utilization of resources imposed by the private industrial monopolies of the pre-WWII era. Lange argued that, therefore, socially motivated public monopolies were superior to the private ones that produced too little, employed too few people, and were able to set prices and quantities.

Consequently, planning and public ownership were not simply solutions to the high prices and rationing of the 1930s or the immediate post-WWII period. More fundamentally, the pre-WWII situation had resulted in the development of a private economy unable to utilize existing physical and human resources. Central planning in a sense aimed to solve a market allocation problem that the pre-war approach to the regulation of incumbent concentrations under the 1933 Polish Act on Cartels had failed to accomplish. The influence of this historical experience on a new generation of Polish lawmakers represents one potential explanation for the relatively restrictive regime adopted and implemented in the 1990s. In comparison, central planning in the Soviet Union started decades earlier in the 1920s. A stronger social memory of the intractable social and economic dilemmas of monopoly capitalism in Poland consequently may have been one factor conducive to the development of a robust competition regime after central planning.

Ironically, by the 1970s the socialist plan had started to exhibit similar rationing and resource underutilization problems to those of the cartel era in the 1930s. This feature of central planning in maturing socialist countries is colloquially captured by the description of such economies as supply constrained, to distinguish them from the demand side problems faced by a Keynesian capitalist economy. In these supply constrained economies, incomes and standards of living were relatively high and equally distributed. However, because of price regulations, demand for some goods and services remained unsatisfied. To meet these economic demands, firm managers started to ask central planners for more autonomy in the management of their affairs, which resulted in some incremental reforms in Poland by the early 1980s.

[32] *Ibid*, p. 167.

In 1981 The Congress of the Polish United Workers Party released guidelines on controlled development of markets and competition.[33] Later the Parliament approved the guidelines relating to merger control in the event of monopoly creation, market segmentation, or price fixing.[34] Antimonopoly policy also aimed to monitor the formation of associations of public enterprises and joint ventures. The 1987 Polish Act on Countering Monopolistic Activities in the National Economy implemented some further elements of the 1981 Congress guidelines and assigned private rights of access to administrative courts and specialized arbitration commissions to file complaints. However, there is little evidence that the pre-1989 substantive norms were employed as policy instruments. The government employed instead the more general 1982 Act on Socio-Economic Planning, Prices, and Financial Management of State-Owned Enterprises, which delegated broad regulatory powers to the Minister of Prices to control monopolistic and other practices viewed to be undesirable from the perspective of the government.

Despite broad discretionary powers, the incremental reforms towards decentralization during this period resulted in supply shortages and unanticipated price increases for consumer goods. Milanovic (1992) documented that between 1978 and 1988 the percentage of population living in poverty increased between from 10 to 20%.[35] He also showed that during this period, the composition of the people in poverty changed. Rural populations and mixed households (farm/non-farm) managed to withstand higher real prices, plausibly because of their higher level of flexibility to contract away from the socialist industrial sector and produce locally. The urban population was most vulnerable to the economic problems.

Collective action by labor gained impetus within the context of the price increases of the early to mid-1980s and culminated in the emergence of the Solidarity movement. Labor protests forced the government to provide a legal basis for the development of "socialist entrepreneurs".

General strikes in 1988 directly resulted in the formation of a new government comprised of a coalition of dissident intellectuals and technocrats. King (2002) argues that the political transition changed the organization of linkages between economic and political elites more radically in Poland than in other jurisdictions such as Russia, for example. The reconfiguration of connections between political and economic elites through the political transition provides a potential explanation for the design of more interventionist competition policies. In many other jurisdictions that adopted competition laws around the

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[33] See Varady (1999), *supra* note 22, for a review of developments in competition legislation prior to the collapse of central planning.
[34] *Ibid*.
[35] Milanovic (1992), *supra* note 3.

same time, incumbent political elites remained in power after the formal shift to a new regime, and hence had control over the design of competition regulations operative during and after the privatization of productive assets.

The political and economic turmoil of the 1980s had resulted in approximately 500 percent annual inflation and 12 percent real GDP contraction in Poland by 1990. This situation motivated the adoption a wide range of fiscal austerity measures, which further exacerbated the collapse in production and employment. A surge in imports resulted in balance of payments problems, and prompted a tariff increase from 5 to 18% by the summer of 1991.[36]

The Act on Countering Monopolistic Practices was debated within this environment and enacted in the February of 1990.[37] Public sector liquidity problems and a deterioration of production and employment conditions in Poland coincided with the formation of the statutory mandate for the regulation of anticompetitive agreements and abusive practices. Similar factors were associated with the enactment of competition laws in other transition and developing countries in the 1980s and 1990s, particularly in Europe and Latin America.

B. Institutional Environment for the Implementation of Competition Law

Continued economic decline in the early 1990s led to new political pressures in Poland. By 1993 the electorate removed the anticommunist dissidents from political power and instituted a government with a strong mandate to create an effective institutional infrastructure for the operation of a market economy. The SDL (formed from members of the United Workers Party) and Polish Peasant Party coalition that came to power after experimentation with shock therapy in 1993 dominated the national legislative and executive institutions during the 1990s, and presided over the adoption of a new constitution in 1998.

Kitschelt and Smyth (2002) find that both governing party elites and the opposition members in Poland had relatively cohesive party platforms for dealing with the economic problems that had emerged in the early 1990s.[38] They further argue that cohesiveness of platforms within parties made yardstick competition

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[36] For an analysis of initial tariff liberalization and drivers of subsequent adjustments see J. Winiecki, *Transition Economies and Foreign Trade* (Routledge, 2002).

[37] Some provisions of the law were amended during the decade through the legislature or by executive order. Unless otherwise stated, this analysis focuses on the version of the act as amended on June 28, 1991. (1990 Act) As detailed below, the mandate of competition authorities was extended in 1996 to incorporate unfair competition and major substantive changes to the legal framework were adopted on December 15, 2000 Act On Competition and Consumer Protection (2000 Act) in order to comply with EU accession requirements.

[38] H. Kitschelt and R. Smyth, *Programmatic Party Cohesion in Emerging Postcommunist Democracies*, 35 Comparative Political Studies 10 (2002), 1228-1256.

among parties easier to observe by voters, hence more effectively mapping social demands into political action. This observation potentially explains why lawmakers supported and monitored the active use of competition law as an instrument of decentralization of the socialist economy, or at least did not block the efforts by the bureaucracy to address concerns before, during and after privatization. The capacity of the political system to channel demand by voters and punish ineffective implementation of the statutes represents another factor in explaining the Polish experience with competition law.

A second, more traditional explanation for the active competition policy stance relates to the price increases that accompanied shock therapy. Competition tends to reduce prices, hence the preference for a more robust competition regime. As detailed in the next sections, competition laws in Poland did not resort to the direct regulation of prices and contracts, but instead focused on controlling abusive practices by incumbent public and private concentrations.

In Poland, as in many other jurisdictions in Central and Eastern Europe, the transition to a market system started with a legacy of large industrial agglomerations and rigid supply chains where each downstream entity purchased its inputs from one or very few suppliers.[39] Kattuman and Domanski (1997) studied the evolution of industrial structures following shock therapy in Poland during the early to mid-1990s.[40] They showed that the high industrial concentration ratios inherited from central planning in fact increased further during the early years of transition. Combined with insufficient entry for the pre-1995 period, Kattuman and Domanski argued that the "overall result of competition policy has been quite the opposite of de-concentration."[41] While their evidence on increased post-socialist concentration in Poland is empirically weaker than that offered by Joskow et al. (1994) for Russia, it reveals the presence of similarly strong incentives for consolidation among enterprises that had, or were going through, a change in ownership and/or management. If concentration facilitates anticompetitive collusion, then the dynamics of the industrial structure likely informed voters and lawmakers about the need for credible legal constraints against anticompetitive practices in shaping the evolving market environment.

Roberts and Thompson (2003) studied the evolution of entry and exit patterns in 152 industries between 1988-1993, shedding light on the interplay between static and dynamic measures of market power and dominance.[42] They

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[39] P. Joskow, R. Schmalensee and N. Tsukanova, *Competition Policy in Russia during and after Privatization*, Brookings Papers on Economic Activity (1994), 301-381.
[40] P. Kattuman and R. Domanski, *Industrial Concentration Under Shock Therapy: Poland in Early Transition Years*, ESRC Centre for Business Research, University of Cambridge (1997).
[41] *Ibid*, p. 12.
[42] B. Roberts, and S. Thompson, *Entry and Exit in a Transition Economy: The Case of Poland*, 22 Review of Industrial Organization 3 (2003), 225-243.

showed that rates of entry into Polish industry were relatively high, resembling those in mature capitalist economies, even before 1990. This suggests a large degree of *de facto* decentralization and liberalization of formal and informal barriers to entry prior to the start of the first major privatization and reorganization policies. After 1990, entry rates increased across a wider range of industries, suggesting that the collapse in production and employment resulted in a relatively rapid market response. Interestingly, they find that patterns of entry and exit were highly dependent on the existing level of concentration, but not on the degree of capital intensity in a particular industry.

Duryasz and Kokoszczynski (1998) document that following capital account liberalization in the mid-1990s, both foreign direct investment and portfolio flows to Poland expanded rapidly.[43] Their analysis suggests that the reduction in interest rates made possible by these flows was a significant factor in promoting market entry and recovery from the shock therapy policies in terms of growth in production and employment.

Separating the impact of regulation against anticompetitive practices from other policies that shaped the formation of a market economy is clearly a difficult task. Importantly however, the literature shows that economic challenges as well as the related policy responses, specifically trade and capital account liberalization, were relatively similar across transition economies in the early 1990s. The primary difference between Poland and countries that have been less successful in building a growing economy in the longer term appears to have been the degree of responsiveness of the political system to economic concerns about the organization of privatization and anticompetitive behavior afterwards.

IV. LEGAL CONSTRAINTS AGAINST ANTICOMPETITIVE PRACTICES, 1990-2000

A. Regulatory Objectives and the Design of Substantive Prohibitions

The 1990 Act on Countering Monopolistic Practices established principles and procedures operative during the 1990s.[44] In contrast to many of the competition laws introduced in the early 1980s and 1990s, the Polish statute did not specify objectives other than counteracting monopolistic practices. This section describes the design of substantive prohibitions relating to anticompetitive agreements and

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[43] P. Duryasz and R. Kokoszczynski Financial Inflows to Poland, 1990-96, 25 *Empirica*, 2 (1998), 217-242.

[44] For sources of legal and policy material see: *Supra* note 7.

abusive practices under Articles 4 and 5 respectively.[45] General exceptions to these rules were outlined in Article 6 and were of a relatively limited nature.

In terms of overall design, the statute did not incorporate provisions on consumer protection, state aid, or public procurement. Instead, it prohibited anticompetitive agreements practices in general terms. It also provided the legal basis for three distinct classes of instruments against monopolistic practices.

- Article 4: Prohibited a wide range of anticompetitive agreements and practices, including setting prices or other contract terms, interlocking directorates, restricting market access or dividing markets.
- Article 5: Specified further prohibitions applicable to economic entities or their combinations with dominance (40% market share under Article 2.7).
- Article 19: Provided for registration of entities with more than 80% market and monitoring their practices.

To implement these provisions, the new law established the Antimonopoly Office (AMO) as the primary enforcer of the rules, and created rights of appeal to a specialized antimonopoly court of administrative decisions. Importantly, Polish lawmakers did not provide an explicit basis for private actions through general-purpose courts as had been envisioned under the 1987 Act prior to political and economic transition. Other basic features of the 1990 law included strict merger notification guidelines and the assignment of wide ranging powers to the AMO to remedy anticompetitive practices through structural and pricing remedies, as well as other administrative orders and fines.

The specialized competition bureaucracy became actively engaged in the early stages of privatization which involved primarily small and medium sized businesses, issuing around 1500 opinions between 1991 and 1995 (Fingleton et al., 1996). Large enterprises were restructured before privatization, suggesting that lawmakers accounted for the possibility that the transition in ownership may not automatically generate a market system that functions well.

Given the AMO's role during privatization, its President became an active participant in government economic policy decision making even though not at the ministerial level. The President of the AMO was appointed by the presiding government, making the office directly responsible to the executive.

With the completion of privatization and the start of negotiations on European Union membership, lawmakers expanded the mandate of the AMO by the mid-1990s to include consumer protection and unfair competition statutes. In

[45] For a discussion of the role of early competition policies in transition economies See J Fingleton, E. Fox, D. Neven, and P. Seabright, *Competition Policy and the Transformation of Central Europe*, (CEPR, London, 1994).

1996 the AMO was reorganized and transformed into the Office of Competition and Consumer Protection (OCCP). The 2000 Act On Competition and Consumer protection harmonized the Polish laws with the requirements of the EU accession process by implementing a more flexible rule-of-reason approach to statutory interpretation.

1. Anticompetitive agreements

Article 4 of the 1990 Act defined nine different types of monopolistic practices that the regulatory regime aimed to counteract. General provisions relating to the regulation of agreements can be divided into two groups:

- Contract regulation: Imposing "onerous" contract terms (Art. 4.1), making contracts contingent on third party performance (Art. 4.2).
- Rules of market conduct: Setting prices or rules for the formation of market prices (4.2.1), dividing a market, restricting access of third parties (Art. 4.2), having the same person combine the functions of director, or member of the board, supervisory council, or audit commission in competing economic entities when they have a combined market share of more than 10% of the market (Art. 4.4), setting quantities (Art. 4.3), and setting contractual forms (Art. 4.5).

Importantly, prohibitions against collusive arrangements and restrictive practices did not involve a clear distinction in the treatment of horizontal and vertical anticompetitive agreements. The design approach of the law contradicts the normative view that effective competition laws should treat vertical constraints in a less restrictive manner than horizontal collusion (see for example Williamson, 1983 and Singh, 2002). The generality of the Polish statute enhanced the scope of the law over anticompetitive vertical arrangements relative to the laws adopted by other post-socialist jurisdictions in the early 1990s such as Russia, for example. As detailed by Pittman (1998), the primary change in competition laws in post-socialist countries in the mid-1990s was to extend a stronger language against vertical agreements following privatization.[46] The 1990 Polish law consequently had a broader scope over anticompetitive agreements than the regulations adopted elsewhere in the region.

The provision on interlocking directorates under Article 4.4 further illustrates the use of bright line rules in this regime. This restriction limited the ability of independent entities to assign agents to direct behavior in other firms, which can be a useful method of monitoring a cartel.

[46] R. Pittman, *Competition law in Central and Eastern Europe: five years later*, 43 Antitrust Bulletin 1 (1998), 179.

Article 6 stipulated that the general restriction under Article 4 applied "unless they are necessary to conduct an economic activity *and* do not result in a significant restraint on competition." [47] It also placed the burden of proof on the "party that claims their existence". Pittman (1998) documented that in practice this formulation made it difficult for an alleged offender of the substantive prohibition to convince the AMO, or the Antimonopoly Court, that both conditions have been satisfied.[48] He also pointed out that in practice the AMO treated cartel agreements as *per se* illegal.

Article 9 of the act stipulated that that AMO may issue decisions prohibiting the implementation of agreements that establish product specialization in the production or sale or provide for joint sales or purchases when such agreements prejudice the interest of other economic entities or consumers. The design of this provision reflects the rule-of-reason approach and stands in contrast to the *per se* prohibitions under Article 4 on price and quantity restrictions, as well as interlocking directorate structures.

2. Concentrations

The 1987 law granted formal authority to the Ministry of Finance to dissolve concentrations if they could lead to a substantial lessening of competition. With the formation of the AMO from staff at this ministry, merger review was delegated to the bureaucracy, but residual price control powers remained at the executive level. With the erosion of price controls and privatization, the competition statute became the primary legal basis for constraining the costs of anticompetitive practices in the emerging markets.

Article 5 of the Polish statutes outlined a number of specific prohibitions relating to firms with a dominant position.[49] These included attempt by dominant enterprises to:

- Counteract the formation of "conditions indispensable for the emergence or development of competition". (Art. 5.1)
- Selling in a manner that "leads to offering privileged status to certain economic entities". (Artic 5.2)
- Refusal to sell and discrimination "when there are no alternative supply sources or outlets". (Art 5.4)
- Unfair influence on price formation, including resale price maintenance and selling below the costs of production in order to "eliminate" competitors.

[47] Emphasis added.
[48] Pittman (1998), *supra* note 46.
[49] Defined as 40% market share in Article 2.7.

The emphasis of dominance provisions on the development of market competition, rather than protecting competition or consumers, highlights the relevance of the laws as part of efforts to decentralize the socialist economy. These provisions enhanced the flexibility of the enforcers in addressing discriminatory or exclusionary behavior in the emerging markets by large enterprises and trade associations.

Article 6 further stipulated that economic entities in a monopolistic position are prohibited from:[50]

- Limiting production, sales, or purchases, "despite having adequate capacity, particularly when it leads to an increase in sales prices or a reduction in purchase prices." (Art. 6.1.1)
- Refraining from sales to increase prices. (Article 6.1.2)
- Charging "excessively exorbitant" prices (Article 6.1.3)

The 1990 Act provided three distinct classes of remedies to control the costs of anticompetitive practices by large entities and their combinations. In addition to the broad discretion to issue administrative orders regulating specialization agreements under Article 9, Article 8.3 provided the AMO with the power to order reductions in prices for specific period of time. The law also implemented a framework for the use of administrative monetary penalties, capped at 15% of annual revenues under Article 14.2.

Varady (1999) stressed the significance of judicial oversight in the formation of regulatory authority for the control of dominance during the early stages of the transition through the example of the FSO Auto case (1990-91).[51] The case involved a ruling by the AMO against the dominant automaker to reduce prices, thus representing an attempt by the competition bureaucracy to use its formal powers to engage in price regulation in the car industry.[52] The Antimonopoly Court disagreed with the AMO and argued that that the AMO must demonstrate a restriction on output in conditions of excess productive capacity to use its price control authority.[53]

On appeal the Supreme Court also ruled against the AMO, pointing out that the government has a wide range of instruments available to influence prices if they are too high including reductions in barriers to international trade.[54] Importantly, the Supreme Court ruling stressed that "the Antimonopoly Law

[50] Defined as 80% market share in Article 19.4.
[51] Varady (1999), *supra* note 22.
[52] Decision No. DO-I-644/37/90/HS of f the Polish Antimonopoly Office, October 24, 1990.
[53] Decision No. XV Amr 7/90 of the Antimonopoly Court, December 12, 1990.
[54] Decision No. II CRN 120/91 of the Supreme Court.

could not be a hidden mechanism for price control." The decision essentially focused the AMO on non-price control instruments for implementing its mandate, which generally included administrative orders and monetary fines. Price control authority during the early stages of transition hence remained with the executive branch, allowing for the specialization of the AMO with respect to identification and mitigation of abusive practices by large incumbent entities.

The law provided the competition bureaucracy with broad authority to regulate ownership of stocks or assets under Article 4.4., "when such acquisition could lead to a significant weakening of competition." Article 11 outlined specific rules regulating mergers. It stipulated that entities aiming to merge must notify the AMO.[55] The AMO was given the power to issue orders prohibiting the "merger, transformation, or establishment of an economic entity" if the resulting entity "would gain or maintain a dominant position" (Art. 11.2). The competition enforcers were given a period of two months to issue a decision prohibiting a merger. A transaction could proceed however under Article 11.3 if the AMO failed to issue an adverse decision with the two month window.

In addition to preventing proposed transactions, Article 12 provided the AMO with the authority to divide or liquidate "state enterprises, cooperatives, and companies under commercial law that have a dominant position on a market", "if they permanently restrain competition and conditions for its emergence." Such a strong threat of *ex post* merger control is consistent with the mandate given to the AMO to promote the development of competitive markets. In contrast to prohibitions against price fixing and vertical restrictions, the merger control provisions relied on the application of the rule-of-reason and case-by-case assessment of dominance and conditions for its emergence. The statue did not provide an explicit efficiencies defense in the treatment concentrations, merger control, and in general exemptions to the prohibitions against anticompetitive practices outlined in Article 6.

3. Unfair competition

This class of substantive norms is often associated with the protection of competition or consumers. These norms were not incorporated in the 1990 Act and did not fall within the competence of the specialized AMO until the creation of Office of Competition and Consumer Protection (OCCP) in 1996. Varady (1999) points out that elsewhere in CEE/FSU this class of rules received a

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[55] Originally, the notification requirements applied to all combining entities (under Executive Order of Council of Ministers of July 11,1990), but in the early 1990s they were modified to be based on sales and asset level criteria denominated in a shadow currency (ECUs before the euro). The content of notification was determined by a resolution at the ministerial level, in particular in the Regulation of the Council of Ministers, July 13, 1993.

relatively small space in formal competition statutes, but represented a large part of enforcement activities by bureaucracies in the early stages of transition.[56]

4. State aid

The 1990 Act similarly did not grant the AMO the competence to monitor state subsidies and preferential treatment in the allocation of state aid. This function remained with the Ministry of the Economy during the early to mid-1990s and was transferred to the OCCP with the EU harmonization process later in the decade. A separate Public Procurement Office monitored the allocation of government purchasing contracts with a value exceeding EUR 3,000 and heard complaints by aggrieved competitors for public funds.

B. Administration and Interpretation

Dutz and Vagliasindi (2000) developed a subjective indicator for the effectiveness of competition policy implementation using a survey of legal experts conducted by the European Bank for Reconstruction and Development (EBRD) in 1999 for 18 CEE jurisdictions including Poland.[57] The indicator is reflective of standards of practice as of 1997. The implementation of Polish competition policy and law ranks first in their index of effectiveness with a score of approx. 6/10 (for reference, the value for Russia stood at 3/10). The authors also looked at the association between the legal index and country level indicators of enterprise mobility capturing the frequency with which firms expand employment.

Three components of policy implementation in CEE – competition advocacy, institutional effectiveness and enforcement – are weighed equally in their index of regulatory effectiveness. Before exploring these elements in the Polish case, it is useful to point out that from the mid-1990s the general allocation of resources to the public administration for all tasks appears to have been stable in terms of human resources, but increasing in terms of the nominal budget (see Table 1). Given the organizational change from AMO to OCCP in 1996, longer-range data are not comparable, and the rest of this section focuses on the practices after this date and prior to the adoption of the rule-of-reason approach in 2000.

[56] Varady (1999), *supra* note 22.
[57] Dutz and Vagliasindi (2000), *supra* note 25.

Table 1 Resources for Public Enforcers in Poland		
	Persons-year	**Budget (Mil. PLN)**
2000	188	12
1999	185	9
1998	180	8
1997	173	7
1996	160	6
Source: OECD (2002)		

1. Competition advocacy

Competition advocacy is typically defined as activities of the administrative agency that aim to advocate the benefits of competition, for example in privatization policy or the regulation of business infrastructure. For the general sample of CEE/FSU, Dutz and Vagliasindi (2000) find no association between their measures of effectiveness of competition advocacy and competition at the cross-country level.[58] The Polish case clearly goes against the grain of their statistical results for the region during this period given the early and deliberate role the AMO was given in monitoring privatization with around 1500 opinions between 1990 and 1995.

2. Institutional effectiveness

Institutional effectiveness is defined by Dutz and Vagliasindi (2000) to include a degree of political independence, transparency, and effectiveness of private appeals against public actions.[59] The procedures set up under the 1990 Act in Poland reveal that the practice of competition law functioned under a good deal of both political and judicial oversight. This observation stands in contrast to the common hypothesis that independence from politicians or courts improves the performance of regulatory agencies. However, a strong pro-competitive stance was part of the policy priorities for the winning SLD coalition in the 1993 elections. As illustrated by the FSO Auto decision, judicial oversight nevertheless separated bureaucratic powers and instruments between the competition bureaucracy and the price regulators at the Ministry of Economy.

Other features that potentially enhanced the institutional effectiveness of the Polish regime include the organization of the AMO under the Ministry of Finance rather than the Ministry of Economy. This choice created some distance between industry managers and public authorities.

[58] *Ibid*.
[59] *Ibid*.

The substantive norms of the 1990s generally allowed a broad scope for action by the AMO, reducing the incentives for appeals. There were no appeals based on dominance provisions in the early years, but this situation has changed significantly since the late 1990s.[60]

3. Enforcement

Dutz and Vagliasindi (2000) found that the level of enforcement activity had a positive association with the economic outcome measure for the region, but with a lower level of statistical significance than the institutional effectiveness indicator.[61] One explanation for this may be the subjectivity of measuring institutional effectiveness based on a non-randomized survey of experts. For this reason, it is imperative to describe competition law practice through an analysis of real patterns of enforcement activity. Table 2 details these patterns following the completion of privatization and the creation of the OCCP.

Table 2
The Practice of Competition Law in Poland, 1996-2000

	1996 A	B	1997 A	B	1998 A	B	1999 A	B	2000 A	B
Horizontal agreements	3	0	12	4	10	1	17	3	19	4
Vertical agreements	4	1	1	1	8	2	3	0	9	0
Mergers	456	16	1191	243	1410	177	882	84	972	64
Abuse of dominance	158	62	189	65	189	65	245	118	274	56
Unfair competition	0	0	22	1	91	10	138	10	235	19

A: Matters opened, B: Sanctions or orders by OCCP
Source: OECD (2002)

In the context of the economic and legal institutions described so far in this analysis, the patterns of practice represented in Table 2 offer a number of interesting inferences. Specifically, they allow us to differentiate between formal proclamations by lawmakers, and the signals and incentives generated by the practice of public enforcement of the substantive prohibitions. The absolute levels of enforcement activity indicate the distribution of resources across different legal instruments available to the bureaucracy. The ratio of investigations to sanction reveals the ability of the competition agency to identify and prosecute

[60] Pittman (1998), *supra* note 46.
[61] Dutz and Vagliasindi (2000), *supra* note 25.

anticompetitive practices accurately based on the customary interpretation of substantive norms at the time.

It is important to note again that monitoring the distribution of state aid was not part of the mandate during the period under analysis here and only became relevant with the EU accession requirements later in the decade. The following discussion characterizes the effectiveness of enforcement starting from the substantive norms that played little part in practice to those that appear more central to the economic implications of the competition regime.

Unfair competition: Until 1996 the AMO did not have the legal competence to implement statutes aiming to differentiate between fair and unfair practices in markets. The data indicate that following the creation of the OCCP public enforcers were reluctant to invest their resources in the implementation of this class of prohibitions. Even as the absolute number of investigations increased with the development of bureaucratic capacity, the ratio of investigations to sanctions remained significantly lower than in the case of remedies targeted at firms with existing structural dominance.

Merger review: The absolute level of merger notifications increased during the mid-1990s following the liberalization of capital markets and reduction in local interest rates. After the global financial crises of 1997 and 1998, the numbers abated somewhat. The absolute levels of merger-related matters opened and sanctioned are somewhat misleading indicators of the practice. This is because activity reports of the OCCP indicate that on an annual basis, around one or two transactions were prohibited and most of the sanctions in the data related to failures of economic entities to adequately notify the authorities of their transactions. In 1999 for example no negative decisions on mergers were issued. After 1996, the bureaucracy appears to have placed merger transactions under a greater degree of scrutiny, illustrative of pressures for increased industrial consolidation following privatization. Overall, the competition authorities do not appear to have implemented competition law as an instrument for controlling industrial structure after the firms were privatized.

Vertical and horizontal agreements: The general substantive prohibitions adopted by Polish lawmakers in 1990 did not differentiate between horizontal and vertical anticompetitive arrangements. In practice, the data indicate that the bureaucracy did not devote its resources to implementing the bright line rules against firms that lack some form of dominance. The data suggests that competition law in Poland did not evolve as an exercise in the direct regulation of contractual terms, but in response to supply bottlenecks arising from anticompetitive practices by managers of incumbent concentrations in the mid- to late 1990s. However, it is important to note that Polish laws restricted the capacity of the same person to serve on boards, supervisory councils, and audit commissions of competing entities when they had a share of more than 10% of the market. This rule restricted the capacity of competitors to employ interlocking directorate structures to coordinate and monitor the behavior of their partners in a cartel.

Abuse of dominance: Although Polish public enforcers did not devote much of their financial and human resources to constraining the range of contractual forms or prevent many mergers, they consistently invested in implementing substantive prohibitions against incumbent concentrations. Importantly, despite the expansion of the range of statutes after 1996, the patterns of bureaucratic practice seem to have persisted and even strengthened in the late 1990s. The OCCP hence continued to specialize in targeting abusive practices by large enterprises even after the lawmakers had increased the complexity of its mandate. In terms of the ratio of sanctions to investigations opened, Table 2 suggests that public enforcers managed to identify illegal activities in one third of cases in a consistent manner. The numbers for 2000 do not reflect this insight, possibly because significant bureaucratic resources were devoted to legislative harmonization with EU requirements during that period.

C. EU Harmonization

In addition to internal economic and political factors, integration with the European Union has also influenced the design of competition law in Poland.[62] The broad language of the substantive prohibitions adopted by Polish lawmakers in 1990 is similar to those under Articles 81 and 82 of the Treaty of Rome and subsequent EU level commitments among the member states relating to the regulation of anticompetitive agreements and abusive practices that restrain internal trade.[63] The agreement signed between Poland and member states (Europe Agreement) in 1991 also incorporated the broad language of EU rules. Specifically, Article 63 of the 1991 Europe Agreement prohibited agreements and practices by undertakings which “have as their object or effect the prevention, restriction, or distortion of competition” that may affect trade between the Community and Poland. The 2000 Act On Competition and Consumer Protection

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[62] For an discussion of internal and external considerations in the design of competition enforcement regimes see R. Rajabiun, *Strategic Considerations in the Emergence of Private Action Rights*, 32 World Competition 3 (2009), 409-434.

[63] Treaty on European Union, 1993 (Maastricht Treaty) further strengthened the role of competition policy as an instrument of enhancing openness to internal trade.

harmonized Polish laws with the demands of the European Commission and member states prior to accession.

In the treatment of agreements, harmonization under the 2000 Act meant the implementation of *de minimis* exemptions to general rules on vertical and horizontal infractions. Harmonization also extended the authority of the OCCP to issue general "block" exemptions to agreements that have benefits in terms of production and distribution efficiencies, as long as they did not impose unnecessary restraints, and eliminate competition in a substantial part of the market (Art. 7). In terms of merger control, the 2000 Act further extended the authority of the OCCP to exempt transactions for industrial or other policy consideration.[64] Increased reliance on standards under the 2000 Act illustrates the erosion of the *per se* prohibitions operative during the formative days of the market system in Poland.

V. MARKET OUTCOMES

The implications of economic recovery and competition law in the latter stages of transition are analyzed next using firm level survey data. Table 3 provides a comparative picture of the capacity of firms to set market prices as captured by responses from managers, owners and accountants of incumbent firms as of 2002-2003.[65] The data in Table 3 represent the percentage of firms that indicated that most of their customers would stop buying from them if they increased their prices by 10%. Correspondingly, a higher number reflects that firms are more likely to be operating in a competitive market.[66]

[64] See: M. Wise, *Review of Competition Law and Policy in Poland*, 5 OECD Journal of Competition Law and Policy 2 (2003).

[65] Total sample size is around 30,000 firms with 500 organizations per country, distributed in a balanced manner across firm size and industry. Source: World Bank Productivity and Investment Climate Database (PICS).

[66] The survey does not explicitly differentiate between the inability to raise prices due to competition and a monopolist operating on the elastic portion of the demand curve. However, pure monopolies are rare, especially in small open economies. In the case of natural monopolies such as utilities, demand is likely to be inelastic and consumers of necessities would be unlikely to be able to stop buying from the monopoly supplier. Therefore, the theoretical ambiguity in the interpretation of the survey data is unlikely to be significant in practice.

Table 3 Price Setting Powers in Comparative Perspective	
Country	Price Setting Power*
Albania	0.29
Armenia	0.26
Brazil	0.31
Bulgaria	0.39
Croatia	0.23
Czech Republic	0.29
Guatemala	0.25
Hungary	0.35
Indonesia	0.4
Lithuania	0.44
Poland	**0.44**
Russia	0.25
Slovakia	0.34
Tanzania	0.42
Turkey	0.21
*Percentage of firms indicating that most customers would stop buying from them in response to a 10 % price increase. Source: World Bank PICS (2002-03)	

Table 3 indicates a relatively high degree of price taking behavior, and thus competitive market conditions, in Poland. Besides competition law, other contributing factors include openness to trade and finance, and the easing of administrative barriers to entry. These policies were nonetheless common across transition and developing countries in the 1990s, and consequently cannot fully explain the divergence in the indicators of market power.

Despite the apparent low levels of market power in Poland, the same survey offers a puzzling result about the perceptions of the costs of anticompetitive practices on business. Specifically, Table 4 documents the cumulative percentage of firm owners and managers who indicated that anticompetitive practices represent a major or severe constraint on the capacity of their organization to grow. Surprisingly, the level of these perceptions in Poland appears relatively high. This empirical puzzle from Poland parallels the situation in other emerging economies where perceptions of anticompetitive practices are low, but real price setting capacity is high (for example Russia or Turkey).[67]

[67] For a discussion of the Russian experience see: R. Rajabiun, *Competition Law and the Economy in the Russian Federation, 1990-2006*, Global Jurist (forthcoming 2009).

Table 4
Significance of Perceptions of Financial and Anticompetitive Constraints on Firm Growth

Country	Anticompetitive Practices	Access to Financing	Financing Price
Albania	0.42	0.14	0.24
Armenia	0.16	0.22	0.29
Brazil	0.57	0.6	0.83
Bulgaria	0.46	0.41	0.51
China	0.24	0.23	0.22
Croatia	0.2	0.25	0.2
Czech Republic	0.2	0.25	0.21
El Salvador	0.45	0.31	0.28
Guatemala	0.57	0.34	0.24
Hungary	0.15	0.22	0.19
Indonesia	0.17	0.17	0.28
Lithuania	0.25	0.18	0.17
Philippines	0.24	0.14	0.23
Poland	**0.32**	**0.33**	**0.52**
Russia	0.15	0.2	0.13
Slovakia	0.12	0.3	0.3
South Africa	0.16	0.13	0.17
Tanzania	0.25	0.48	0.58
Turkey	0.23	0.17	0.28

Source: World Bank PICS, 2002-2003. Percentage of firms who ranked a particular institutional constraint as major or severe to their growth.

This evidence suggests that the type of markets that emerged in Poland generated better information about anticompetitive practices and increased awareness about business risks caused by them. In order to check the robustness of the results about the level of price setting powers and perceptions of anticompetitive practices, the following tables decompose the countrywide indicators based on firm size, sector and ownership characteristics of respondents. In addition to Poland, data for the Russia are provided for comparison.[68]

[68] Firm level surveys illustrate the presence of a dissonance between perceptions and reality in some jurisdictions, including Poland and Russia. Relatively low perceptions of the costs of anticompetitive practices are complemented by low perceptions of constraints posed by mechanisms for raising external financing for a firm. For an analysis of financial and legal

Table 5 Price Setting Powers by Firm Size, Industry, and Ownership		
Firm Size	**Poland**	**Russia**
Micro	66	50
Small	50	41
Medium	59	39
Large	38	32
Very Large	47	37
Manufacturing	55	36
Services	53	44
Construction	39	39
Exporter	54	29
Non-exporter	54	40
Dom. Ownership	33	21
For. Ownership	60	83
Source: World Bank PICS. Percentages of respondents who indicated many of their customers would stop buying from them if prices were raised by 10% (2002-2003).		

Table 6 Perceptions of Anticompetitive Practices by Firm Size, Industry, and Ownership		
Firm Size	**Poland**	**Russia**
Micro	32	18
Small	32	11
Medium	37	21
Large	34	18
Very Large	32	16
Manufacturing	33	18
Services	31	13
Construction	40	17
Exporter	30	15
Non-exporter	33	16
Dom. Ownership	33	16
For. Ownership	30	11
Source: World Bank PICS. Percentages of respondents who identified anticompetitive/informal practices to pose a major constraint to their growth (2002-2003).		

While the decomposition suggests the presence of a strong size and ownership effect in the price setting capacity of firms in both jurisdictions, the overall results remain the same. The dissonance between perceptions and reality clearly does not seem to depend on the specific features of a business. While

institutions see: T. Beck , A. Demigguc-Kunt, and V. Maksimovic, *Financial and Legal Constraints to Growth: Does Firm Size Matter?* 60 Journal of Finance 1 (2005), 137-177.

price-setting powers in the construction sector were relatively similar in these two economies, the capacity of manufacturing and service firms to extract super-normal rents from buyers was significantly lower in the markets that emerged in Poland during the transition process.

VI. CONCLUSIONS AND POLICY IMPLICATIONS

In conjunction with regulatory policies aiming to enhance openness of national economies to trade and capital flows, a large number of developing and transition countries adopted competition legislations over the past three decades. Recent cross-country studies have failed to identify a direct link between indicators of law and mark-ups or productivity growth, either positive or negative. However, Kee and Hoekman (2007) have documented that the adoption of laws against anticompetitive practices enlarged the number of participants and indirectly constrained industry mark-up levels.[69] Moreover, Voigt (2008) has found that that competition laws may enhance the quality of broader economic and political institutions and indirectly increase total factor productivity.[70]

This paper has suggested one possible reason for the lack of measurable impact of legal indicators might be that the new competition laws were not designed to function as a set of clear, predictable, and enforceable rules against anticompetitive agreements and practices. The flexibility of the first generation of competition laws, as evidenced in the multiplicity of objectives or the availability of the efficiencies defense, may nevertheless have some strong economic justifications. In general, the implementation of excessively rigid rules might deter structures and practices that would be welfare enhancing. In the absence of informational costs and regulatory capture, it is possible to imagine that an optimal competition regime would aim to balance competition and coordination incentives with respect to the requirements of specific sectors in interpreting prohibitions against anticompetitive practices.

The case-by-case approach to the design of competition regulations however has a number of disadvantages. First, it assumes that information required for effective regulation is freely available, and that it can be interpreted in a consistent manner by competition authorities. Second, such a design feature makes it difficult for market participants to form consistent expectations about the boundaries of permissible conduct. Finally, public laws often work when private parties learn to incorporate them in their private contractual relationships. Uncertainty associated with an *ex post* balancing of multiple objectives or establishing an efficiencies defense makes it difficult to employ public

[69] Kee and Hoekman (2007), *supra* note 8.
[70] Voigt (2008), *supra* note 12.

competition laws as a means of "completing" private contracts in the presence of transaction costs to decentralized bargaining. In contrast, *per se* prohibitions appear less prone to information problems and undue influence. Furthermore, in the absence of trust, bright lines against acts such as price fixing can be readily employed to structure private transactions with third parties.

This analysis conjectured that the design of competition laws played a part in explaining divergent paths of long-term development following the collapse of central planning in Central and Eastern Europe. Focusing on the experience in Poland, the study highlighted the importance of early design choices on the manner in which competition regulations shaped emerging market institutions. The decision by lawmakers in 1990 to employ *per se* prohibitions (bright line rules), rather than replicating the rule-of-reason approach promoted by external advisors, distinguished the Polish regime from other transition economies. Responsiveness of the political system to the collapse in production and employment provided support for the active application of these rules during and after privatization.

This analysis does not claim that divergence of formal prohibitions can directly, or fully, explain the distinctive paths of post-socialist development. However, there are two important reasons not to dismiss the implications of the Polish experience for the design of competition regimes that can function as instruments of development policy. First, the initial conditions of the economies in the region were relatively homogeneous at the start of the events detailed here in the case of Poland. Second, broad economic policies, specifically those aiming to liberalize trade and capital flows, were also similar.[71] Consequently, it is plausible to suspect that the heterodox design of competition laws complemented the benefits of openness and enhanced the institutional capacity for the operation of markets. Firm level surveys substantiated the association between *per se* prohibitions and the development of market institutions that restrict the price setting powers of incumbent entities.

The experience detailed here supports the hypothesis by Kovacic (2002) who argued that a central problem with the effective implementation of competition laws elsewhere in the region had been their excessive complexity.[72] As documented by Pittman (1998), some post-socialist countries that did not adopt *per se* prohibitions on cartel arrangements, vertical restrictions, and

[71] Although most countries rapidly liberalized external trade, balance of payments problems resulted general tariff increases in the early 1990s. Trade policies started to diverge by the mid 1990s across the region and tariff peaks started to emerge. See Winiecki (2002), *supra* note 34, for a discussion of trade policies in transition countries in the early to mid 1990s. For an empirical analysis of trade policy formation in Poland in the late 1990s see J. Jagemejer and J. Michalek, *The Political Economy of Poland's Trade Policy: Empirical Verification of the Grossman-Helpman Model*, 46 Eastern European Economics 5 (2008), 27-46.

[72] Kovacic (2002), *supra* note 24.

interlocking directorate structures, had to indeed strengthen relevant legal prohibitions in the mid- 1990s.[73] In other jurisdictions, the adoption of a more restrictive regime using *per se* prohibitions faced significant political resistance in the formative days of the market system. In the Russian Federation for instance, lawmakers finally repealed the rule-of-reason approach to the interpretation of anticompetitive agreements and adopted *per se* prohibitions against collusion in 2006 with the adoption of The Federal Law on the Protection of Competition (135-FZ). However, the Russian laws continue to allow for an efficiencies defense in the treatment abusive practices by dominant firms, which is common in the model of competition laws replicated by most transition and developing countries in the 1980s and 1990s.[74]

In the broader comparative context, the emphasis on the simplicity/complexity of substantive prohibitions is particularly relevant because most jurisdictions that adopted new competition laws, designed them as regulatory instruments aiming to balance competing objectives. As noted earlier, contemporary national competition statutes incorporate on average three and a half additional objectives beside protecting or promoting competition. Common among these secondary objectives are the promotion of vaguely defined ideas such as economic efficiency or international competitiveness. Observers of competition law in the United States and the European Union have also noted a trend in increased application of the rule-of-reason approach to interpreting substantive prohibitions. Evidence on the design of the competition regime in Poland suggests that simply replicating this trend may not be an optimal strategy for all jurisdictions that aim to employ competition law as an instrument of development policy.

With respect to the organization of regulatory mechanisms, it is important to reiterate that the 1990 Act complemented the restrictive substantive norms with a narrowly tailored mandate for a separate competition bureaucracy. The competition bureaucracy (AMO and OCCP) also strategically focused its resources on combating abusive practices by large incumbent entities and constraining incentives for excessive consolidation in the privatized economy. Significantly, top-down monitoring by elected politicians, as well as judicial guidance about the range of civil and administrative remedies available to the bureaucracy, shaped active enforcement of substantive prohibitions by competition authorities.

The experience suggests that limiting the range of remedies available to competition enforcers may be a desirable feature, potentially because it stimulates bureaucratic specialization. Importantly, the evidence from Poland casts doubt on the desirability of formal or informal rules separating regulators from politicians.

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[73] Pittman (1998), *supra* note 46.
[74] Rajabiun (2009), *supra* note 67.

Indeed, it appears that the regime was relatively effective in constraining emerging concentrations in the post-privatization period precisely because political institutions channeled economic demands into a relatively restrictive regime against abusive practices in the emerging market system. Importantly, the public enforcers did not implement competition law in terms of price regulation or try to control market structure. Regulatory independence consequently does not seem to be a necessary ingredient in the effective use of competition law as an instrument of development policy, a result consistent with recent cross-country evidence.[75]

While the Polish experience highlights the importance of credible rules against anticompetitive practices for long term development outcomes, it also raises further questions about specific channels through which such institutions influence economic interactions. Specifically, the survey data detailed in the last section suggested that although emerging market institutions in Poland effectively constrained the price setting capacity of incumbent entities on a comparative basis, perceptions of the costs of anticompetitive practices were relatively high. A parallel dissonance between perceptions and reality of market power is also evident in jurisdictions with distinctive paths of economic development such as Russia or Turkey. If awareness of the risks involved in market conduct is necessary for making individually rational decisions, then the evidence from Poland suggests that effective competition regulations not only constrain anticompetitive practices, but also help inform market participants about their costs.

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[75] Voigt (2006 and 2008), *supra* note 12.

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