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*Israel**

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Israel, established in 1948, is located in the Middle East, and borders Egypt to the South, Lebanon and Syria to the North, Jordan to the east and the Mediterranean Sea to the West. In 2003, it was estimated that 76.6 percent of the Israeli population were Jewish. The non-Jewish population consisted mainly of Arabs of the Sunni Muslim denomination (15.7 percent) and Christians (2.1 percent). The most common languages spoken in Israel are Hebrew, Arabic (official languages) and English.[1]

Economy

Israel has a small, yet technologically advanced market economy. It is, for the most part, an open economy, with high export and import levels, and high levels of research and development activities.

In the last two decades, the Israeli economy has been radically transformed from one largely based on agriculture and low-tech industries, such as textiles, to one relying, to a large extent, on high-tech industries.

In 1992, citrus fruit (Israel's leading export at the time) and software exports were each worth around US$125mn. By 2001, citrus exports had basically remained stable, whilst software exports had jumped to US$3.5bn.

Exports from hi-tech industries have constituted, in recent years, more than half of Israel's industrial exports. This transformation has been partly facilitated by changes in the regulatory framework.

Since the late 70s, the Israeli economy has undergone a process of deregulation, privatisation and liberalisation, which has opened up many of its markets and has significantly increased foreign direct investment, as well as export and import levels. At the same time, however, some sectors are still characterised by substantial government involvement, either by way of direct public ownership or by way of regulation.

PROFILE	
Population:	6.7 million***
GDP (Current US$):	103.7 billion**
Per Capita Income: (Current US$)	16,020 (Atlas method)** 19,530 (at PPP.)**
Surface Area:	21.06 thousand sq. km
Life Expectancy:	79.1 years**
Literacy (%):	95.3 (of ages 15 and above)**
HDI Rank:	22 ***

Sources:
- World Development Indicators Database, World Bank, 2004
- Human Development Report Statistics, UNDP, 2004

(**) For the year 2002
(***) For the year 2003

Competition Evolution and Environment

Israel's RTPs Act 1959 (the first Act) was enacted only 11 years after the country was established, at a time when it was trying to create an economic infrastructure to serve a small, developing, and immigrant country, whilst combating formidable monetary and security problems.

To do so, the Government adopted a highly interventionist, centralised and paternalistic industrial policy that regulated almost all aspects of economic activity. Emphasis was placed upon construction, expansion and stability. The market was likened to an infant, who cannot walk on his own and who has to be directed so that he would eventually learn to walk.

Since the belief in the market's invisible hand was very limited, the Government held the reigns of the market, *inter alia,* by controlling import certificates; providing monetary funding to economic activity that it deemed beneficial; granting exclusivity rights to some producers and suppliers; and by directly controlling prices and trade conditions of many goods and services.

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1 http://www.cia.gov/cia/publications/factbook/geos/is.html and http://www1.cbs.gov.il/shnaton55/sto2_01.pdf

As a result, competitive conditions in the Israeli market were very limited. Free competition, it was believed, would have prevented the establishment of efficient domestic firms and would have destabilised the market. Free competition was also often considered unfair. It is not surprising, therefore, that in such an environment the first Act had very little effect on the economy.

This raises the question of what role a competition law has to play in such an environment: How does a competition law apply when prices are controlled by direct price control rather than by market forces; where investment decisions are indirectly subject to approval by Government officials; or where joint ventures between potential competitions are supported by the Government in order to achieve scale economies and prevent market destabilisation?

Little weight was given to competitive considerations. Rather, competition law decisions mirrored the existing ideology by broadly interpreting the public interest exception that was included in the law, and by placing an emphasis on nationwide goals, such as the encouragement of export, the realisation of scale economies, and the improvement of the country's balance of payments.

Accordingly, the Competition Tribunal, (the Tribunal), a judicial body comprised of a district judge and public representatives, that could approve the agreement if it served the public good (interest), ordinarily approved agreements amongst competitors, which had the potential to increase productive efficiency by designating the production of different types of products to different firms.

It also approved many agreements, which were geared towards an increase in exports, even if the effect was increased dominance in the Israeli market. Its decisions were, thus, usually a reflection of governmental policies, giving priority to numerous industrial policy considerations over free competition (Gal, 2005).

It was since 1976, together with the ascendancy of a new Government, when the socio-economic ideology of the Israeli Government changed significantly and a more liberalised approach was adopted, that the 1959 Act began to have a significant effect on the Israeli economy.

The new regime supported the reduction of Governmental involvement in the markets. But the significant change in governmental policy occurred in 1985, as parts of an attempt to rescue the economy from a severe economic crisis.

Following the crisis, the Government made several important policy decisions, including the privatisation of several large companies, the reduction of subsidies, and the liberalisation of the capital market. The changes were not immediate, as it took several years for them to be fully applied. For example, the reform in the capital market began in 1985, but accelerated only from 1990-1995, when Israeli firms were, for the first time, allowed to use foreign funding.

In addition, most Israeli markets were opened to imports. In 1988, as part of the change towards a more competition-oriented economy, the first Act was replaced by the RTP Act 1988, which gave the regulating authorities more power to enforce the law, as elaborated below.

Today, free competition is considered an important value by the Israeli legal system. This is reflected in a recent decision, in which the Chief Justice of the Supreme Court referred to the RTP Act as '*the Magna Carta of consumer rights and free competition'*. However, as noted previously, competition was not always placed on a high pedestal. The history of the Israeli Act, as it is, demonstrates the two-way connection between the governing ideology and the enforcement of a competition law (Gal, 2004a).

It is interesting to note that the history of the Israeli competition law resembles, in many respects, those of many West European states, who also made little use of their competition laws until around a quarter of a century ago, due to centralist and protectionist industrial policy (Gerber, 1998).

The history of Israeli competition law also exemplifies the effects of the institutional and organisational features of its enforcement bodies on the enforcement of the Law. For many years, the members of the Antitrust Tribunal (the adjudicative body set up under the first Act, comprising of a district judge and public representatives) lacked economic qualification, a fact well reflected in many of its decisions.

Further, the Antitrust Authority, which was the body charged with seeking violations of the law and presenting

Box 13.1: Israeli Banks – Coordinated Closing Hours on Friday Mornings

The Tribunal's decision in AD 1393/96 Mortagee Adanim Bank *vs*. Israeli Consumers Authority and others nicely exemplifies the change that occurred in Israeli antitrust enforcement and the shift towards economic analysis.

Israeli banks requested a coordinated closure of all banks on Friday mornings. They argued that such coordinated closure would enable them to cut their costs and thus increase productive efficiency.

The Tribunal rejected the request, based on a complex economic analysis, derived from the game theory, which analysed and compared the effects on public welfare in case the coordinated closure was approved and in case it was rejected.

the case on behalf of the public to the Tribunal, did not have the resources or the incentives to further competition. The Authority was, until about a decade ago, an integral part of the Israeli Ministry of Commerce and Industry (the Ministry), which strongly believed in market intervention.

The General Director of the Authority himself was appointed from the ranks of the Ministry, and in reality presented the views of the Ministry when arguing in front of the Tribunal. This institutional framework was based on the view that the RTPs Act was an integral part of a wider economic governmental policy (MOTC, 1980).

Given this background, along with the fact that the Authority suffered a significant shortage of personnel and other investigative resources and had to rely on the Ministry for such resources, it should come as no surprise that the enforcement of free competition in Israel was very limited (Gal, 2004a; Gal 2005).

Competition Regulation, Institutions and Anticompetitive Business Practices

Before 1959, Israeli antitrust rules, like many other Israeli laws at that time, followed the British common law traditions. Such laws were very different from those that govern antitrust today, in that they only dealt with monopolies, which were the result of exclusive concessions granted by the government to private parties. Besides, with regard to restrictive agreements, they focused upon the injury sustained to the freedom of trade of the contracting parties. Consequently, claims of restrictive agreements were only allowed when raised by parties to such agreements, whose freedom of trade had been restrained, and limited weight was given to the public interest.

The first Act was enacted in an early stage of Israel's economic development, as a response to a public outcry against private cartels, which frustrated the limited attempts to liberalise some parts of the Israeli economy. The first Act contained provisions regarding monopolies and restrictive agreements. The monopoly chapter granted the Minister of Commerce and Industry the authority to supervise and regulate monopolistic behaviour, including the authority to regulate prices, and production and supply methods, where such prices and methods were against the public interest.

The chapter on restrictive agreements contained a wide prohibition against such agreements. At the same time, it also contained several wide exemptions, some of which reflected the interests of interest groups, which succeeded in affecting the legislature.

The first Act also created a system, by which an agreement in restraint of trade had to be registered with the Antitrust Authority. The Authority would then bring any agreement that restricted competition before the Antitrust Tribunal, which could approve the agreement if it served the public interest. Agreements, which were not approved, were deemed illegal.

Box 13.2: Government Promotes Restrictive Agreement in the Plywood Market

A good example of the Antitrust Tribunal's approach towards restrictive agreements, in the sixties, can be found in AC 202/240/5 *Israel Plywood vs. The General Director of the Competition Authority* - (District Court Decisions 48, p. 158).

The decision concerned a restrictive agreement amongst all Israeli plywood manufacturers that fixed prices, designated quotas, and created a system of joint distribution of their products. The Tribunal approved the agreement, in accordance with the recommendation of the Minister, on condition that the plywood produced for local market consumption is sold at prices approved by the Minister, and that the manufacturers commit to an import and export programme designed by the Minister.

It reasoned that the agreement was necessary to increase exports of plywood and to increase productive efficiency, even at the cost of increased prices for local consumption. This case exemplifies the way governmental supervision of the markets was favoured over free competition.

The first Act did not regulate mergers, since mergers were considered a positive phenomenon at that time, allowing the merging firms to enjoy advantages of scale economies, which were essential for increasing productive efficiency in Israeli markets and for successfully competing against foreign competitors.

The climatic change of the 1980s was a critical catalyst for the enforcement of the competition law. In 1988, the first Act was replaced by a newer version. The chapters concerning monopolies and restrictive agreements were not significantly changed, except for relatively minor changes, which gave the enforcement bodies more flexibility when applying the law.

The new version included a chapter on merger regulation, which was based on a recommendation made by a public committee. The law forbids firms from merging without the approval of the General Director of the Antitrust Authority, if the merger meets one of the thresholds set in the law (based on concentration rates or economic turnover). The 1988 Law also states that the Director should condemn the merger if it harms consumers or competition. For its enforcement, the law creates three parallel tracks (IAA, 2004):

- *Criminal enforcement:* The Act contains criminal sanctions for the breach of its prohibitions. Through the years, criminal sanctions have become more severe, and they include imprisonment of up to five years and high fines;
- *Civil enforcement:* Breach of the Act's prohibitions is considered a tortuous act, thus allowing the injured party to initiate civil proceedings, including class actions, against the wrongdoer; and
- *Administrative enforcement:* The law empowers the General Director of the Antitrust Authority to prohibit certain types of conduct that harm competition, as well as the right to declare that a certain conduct is legally prohibited.

These climatic and ideological changes triggered a revolution in the enforcement of the Act. Since the beginning of the 90's, the General Director and the Tribunal began to give considerably more weightage to competitive considerations. Both applied a long-term dynamic economic evaluation of the relevant markets in light of its conditions, such as barriers to entry and market concentration rates. In the span of only a few years, a large corpus of decisions, based on economic analysis, was created and enforcement rates rose significantly.

This change was also enabled by structural changes within the enforcing bodies. In 1993, the Antitrust Authority was detached from the Ministry and was granted an independent status. It also received increased funding and personnel and began to employ its own economists. In 2004, for example, the Antitrust Authority enjoyed a budget of US$4.4mn and employed 78 employees (IAA, 2004).

Additionally, hearings of all criminal cases based on the 1988 Act were designated to a special district judge. This change was a significant one, since one of the main problems in the past was that antitrust cases were heard by judges who lacked the required knowledge in this field of law.

Sectoral Regulation

Israeli markets are regulated by sector- specific legislations. For example:

- The Telecommunications Sector is regulated by the Bezeq Act, which authorises the Israeli Communications Minister to regulate the communications markets, including the authority to grant licences and concessions.
- Israeli banks are subject to the regulation of the Banking Ordinance 1941, and other regulations enacted in order to prevent abuse of power and to ensure stability in the banking system.
- Israeli Insurance Companies are subject to the Insurance Contract Act, 1981, which regulates the relationship between insurance companies and consumers.

As mentioned above, some major companies are still government-owned. The Israeli Government is currently undergoing another phase of privatisation, which includes partial privatisation of several firms, including Bezeq – the Israeli Telecommunications Company, and Zim – the Israeli Navigation Corp.

It is also taking some steps towards creating structural changes in several Israeli monopolies, in order to increase the industry's efficiency and competitiveness. These include*, inter alia*, Mekorot – the Israeli water company and the Israeli port authority, which will hopefully be split into three different firms.

Consumer Protection

The Israeli *acquis* contains various laws legislated for the protection of consumers, the first and most important being the Consumers Rights Protection Act 1981, which includes, *inter alia*, the following articles:

- Prohibition against misleading consumers, including misleading advertising;
- Obligation to disclose relevant information to the public concerning its products and protection against fraud in specific transactions;
- Regulation of product labelling; and

Box 13.3: Joint Distribution of Polyethylene Covers

This change can also be exemplified by the decision in the case of Request for Exemption from Court Approval for Agreement to Establish Poligar (in *Antitrust* (Tel Aviv: Bar Association, 1994), vol. A, 108.) There, the Antitrust Authority was requested to approve a marketing joint venture between the only two Israeli producers of polyethelene covers.

In analysing the effects of the proposed venture, the General Director stressed the disciplining effects of potential and existing imports, on the market power of the domestic firms. He approved the venture since it would enable the domestic firms to reduce their costs and thus compete more effectively with foreign importers, without harming the Israeli consumer.

This reasoning differs significantly from that on which past decisions to approve joint ventures was based. Whereas, in the past, emphasis was placed on the ability of the parties to the venture to reduce their costs without a real analysis of total welfare effects, the decision in Poligar approves the venture based on the need of the parties to act more efficiently in order to meet foreign competition.

The analysis ensures that the Israeli consumer, as well as the Israeli firms, will enjoy the benefits of the venture. This sort of analysis, which gives much weight to competitive considerations, based on market conditions, and evaluates the effects of the conduct on all market players, characterises most of the decisions from the 90's onwards.

- Regulation of indirect sales involving no direct contact between seller and buyer in, which the seller contacts the buyer through telephone or other electronic means without examination of the goods or services by the buyer.

The Director of Consumer Protection is responsible for enforcing the Consumer Rights Protection Law of 1981. He is also authorised, by the Uniform Contracts Law, to require the examination of uniform contracts by the Uniform Contracts Court, to ensure that a powerful entity does not apply its market power over small and dispersed consumers, by including exploitative or misleading clauses in its uniform contracts. The 1981 Law applies to all sectors of the economy, except banking and insurance.

To enhance consumer protection, the Israel Consumer Council was established by the Ministry of Industry, in coordination with the Standards Institute. The Council is a governmental body. Its main goals are to:

- improve consumer protection by preventing consumer fraud and unfair terms in the conditions of sale or lease of goods and services;
- represent the consuming public or a particular sector in dealing with the government and its authorities or any other public or Government body, including the Israeli Parliament and the courts; and
- increase consumer awareness and to encourage consumers, through advertising and counselling, to stand up for their rights.

Concluding Observations and Future Scenario

Despite the significant leap in the enforcement of the 1988 RTPs Act, Israeli competition law has still a long way to go. For one, the Act is poorly worded, some of its prohibitions are drafted too widely and others too narrowly. This has triggered some problematic interpretations by the courts (Gal, 2004b; Israeli, 2005).

As the law is currently framed, all agreements that have a potential to harm competition must be exempted by the General Director or approved by the Antitrust Tribunal, before it comes into force. Other courts are not allowed to approve the agreement, even if its potential harm to competition is small, with the result that such an agreement should be declared null and void.

As a result, some private parties have sought to use the Act as a basis for infringing their contracts. This has led to some unfortunate interpretations of the Act that were intended to overcome this problem, yet may harm the public good in future cases.

The Israeli Antitrust Authority (IAA) made an attempt to narrow this problem by drafting several block exemptions for certain sorts of restrictive agreements in, which anticompetitive influence is not obvious (IAA, 2001). Recently, an expert committee was established in order to recommend changes in the 1988 Act.

Nevertheless, the law's main Achilles' heel is oligopolistic coordination. In a small economy, such as Israel, oligopolistic coordination is widespread and significantly affects economic welfare (Gal, 2003). Yet the law, like most other competition laws in the world, does not provide sufficient tools to curb this phenomenon (Gal, 2003; Israeli, 2004).

What are the lessons to be learnt from the Israeli experience? Most importantly, that competition law does not stand alone. The prevailing socio-economic ideology and public policy are determining factors in the application of a competition policy. Without the elimination of governmental barriers to competition, and a real change in public policy, it is not possible to create a level playing field in which firms will invest and compete effectively.

It is, thus, imperative that the Government truly and consistently accept the principles of competition in all of its spheres: the judiciary, the Government and the legislature, for the competition law to be effectively implemented. Competition law, of the kind known and accepted in most developed economies, could only bloom in a society, which is based on the belief in the benefits of the market's invisible hand over direct regulation, at least in most of its markets (Gal, 2005).

Suggested Readings

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