

VERSENY TÜKÖR

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Pünkösty András*

Frank Hyneman Knight : The Ethics of Competition

Reflections on the recently re-emerging questions concerning the aims of competition and its ethical background

The actual relevance of Professor Frank H. Knight's (1885-1972) intellectual legacy may be more important than ever, given the recent emergence of a new discourse regarding the further aims of competition, beyond its traditionally interpreted economic benefits. Some argue that competition policy and enforcement should promote "fairness"¹, while opponents deem this approach as being populist in nature.² The aim of this review on Professor Knight's early essays, which were republished³ in a book titled "The Ethics of Competition" in 1997, is to draw attention to the thoughts of a central figure of neoclassical economics in the hope that this may help us to understand the recent debate on competition policy in a broader context.

As a mentor of Milton Friedman and George Stigler⁴, Professor Knight was one of the founding contributors of the Chicago school of economics. However, his views were rather complex since he promoted individual economic freedom, claiming that exchanges in a free marketplace are mutually advantageous, yet he believed in markets only because all the alternative options were worse.⁵ As Richard Boyd notes, Knight was one of the central personalities of neoclassical economics of the twentieth century, even though he was also one of the most searching critics of the assumptions and scientific aspirations of neoclassical economics in the history of the discipline.⁶ Today, a wide range of literature has been published to support antitrust policy

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1 For instance, see the opening remarks of the Acting Assistant Attorney General Renata Hesse of the Antitrust Division, delivered at the 2016 Global Antitrust Enforcement Symposium: And Never the Twain Shall Meet? Connecting Popular and Professional Visions for Antitrust Enforcement, Washington, DC, September 20, 2016. <https://www.justice.gov/opa/speech/acting-assistant-attorney-general-renata-hesse-antitrust-division-delivers-opening>, or Lewis Crofts and Matthew Newman: Vestager's 'fairness' mantra rattles through EU competition law <https://mlexmarketinsight.com/insights-center/editors-picks/antitrust/europe/vestagers-fairness-mantra-rattles-through-eu-competition-law>

2 Maurits Dolmans – Wanjie Lin: Fairness and competition law: A fairness paradox *Concurrences* N° 4-2017. 1.

3 Frank Hyneman Knight: *The ethics of competition*; with a new introduction by Richard Boyd, New Brunswick, N.J., USA: Transaction Publishers, 1997.

4 For the sake of completeness, we should note that the preface of the original version of the book (1935) was written jointly by Milton Friedman, Homer Jones, George Stigler and Allen Wallis. The idea to publish the book arose during a dinner to celebrate Professor Knight's forty-ninth birthday.

5 https://www.lib.uchicago.edu/projects/centcat/centcats/fac/facch23_01.html

6 Richard Boyd: Introduction to the transaction edition, *Frank Hyneman Knight: The ethics of competition*; with a new introduction by Richard Boyd, New Brunswick, N.J., USA: Transaction Publishers, 1997.vii.

from a theoretical perspective, and it is now quite obvious that the assumptions of the perfect market, one of the essential elements of the neoclassical school, are faulty; nevertheless, it is still worthwhile taking a closer look at a classical paper⁷ that investigates the heart of competition from a broader ethical perspective.

The content of the book demonstrates that a highly detailed and comprehensive approach was taken when considering competition policy. The eleven chapters⁸ of the book were initially individually published papers in the 20s and 30s, and reflect on many areas of competition policy. In the first chapter, Knight examines the problem of Ethics and the Economic Interpretation and discusses the scope and the methodological difficulties faced when interpreting the subjects from both ethical and economic points of view. He raises the question as to whether human motives are predominantly economic, or whether they are predominantly instinctive? In this first chapter of the book, Professor Knight introduces a possible framework of ethical interpretation by referring to the main ethical traditions.

The primarily purpose of this current review is to take a closer look at the second chapter, which the book was eventually named after – The Ethics of Competition. Professor Knight addresses at the outset the value problem in economic policy and expresses the necessity of formulating ideals from an “absolute ethics” point of view. Professor Knight then states that an examination of the competitive economic order from the standpoint of its ethical standards can be divided into three parts. The first part considers the contrast between the theory and practice of *laissez-faire* individualism, as regards to the want-satisfaction problem. The second part consists of an analysis of business as a game (the elements of a game and criticism of the business game). Finally, he investigates the basic motives behind competition and evaluates these motives from a *pure ethics* point of view. The main ideas of these three sections will be briefly summarised below.

But first of all, by formulating the central position of the *value problem* in economic policy, Knight addresses the want-satisfaction problem, which he also subdivides into three points. Although the wants are not ultimate data nor are they to be identified with values, we can never get entirely away from physical needs, for example relating to the requirements for life and for health and comfort, as such motives link to civilised behaviour and current societal expectations set minimum requirements for these needs. The first question is *which* wants and *whose* wants are to be satisfied -- and the (economic) system's answer to this question constitutes its social economic values scale. This leads to the old problem of social justice relating to the system's treatment of the wants of persons and classes. The second value standard is more mechanical, but is still a problem of values and deals with the *efficiency* of the system “in using its available resources in creating the values which it recognises, that is, in producing the largest quantity of ‘goods’ as measured by the standards which it sets up”. As to the third point, Knight points out that the wants which an economic system operates to gratify are largely produced by the workings of the system itself. In organising the value scale, the economic order influences the formation, if not the outright creation of the wants themselves – so the wants, as well as the means of their gratification, are largely the product of the system. Resultantly, the examination of the ethics of an economic system must take into account the kinds of wants that it tends to generate or nourish, as well as its treatment of wants as they exist at any given time.

After considering the value problem in economic policy in general, Knight structures this chapter into three main sections following the three central points of inquiry already mentioned above. Firstly, he examines the contrast between the theory and practice of *laissez-faire* individualism, as regards to its value scale and organisation of resources to product values and in its distribution of produce.

7 Frank Hyneman Knight: The ethics of competition, Quarterly Journal of Economics, The University of Iowa, May, 1922. 579-624.

8 The chapters are the following. 1. Ethics and the Economic Interpretation, 2. The Ethics of Competition, 3. Economic Psychology and the Value Problem, 4. The Limitations of Scientific Method in Economics, 5. Marginal Utility Economics, 6. Statics and Dynamics 7. Cost of Production and Price over Long and Short Periods, 8. Fallacies in the Interpretation of Social Cost, 9. Value and Price, 10. Interest, 11. Economic Theory and Nationalism.

This section mainly refers to the argument for individualism, as developed by its advocates from Adam Smith down⁹. Professor Knight provides a detailed criticism of its basic principles and explains why he thinks that the competitive system, viewed simply as a want-satisfying mechanism, falls far short of the highest ideals. Knight observes that even though the position is entirely sound, it is not a statement of a sound ethical social ideal, but a specification for a utopia. While the arguments that Professor Knight summarises in 12 points may be familiar to readers, given the fact that it is quite obvious that the perfect market is rather a theoretical option, the manner in which he synthesises his critique with an ethical perspective is captivating.

The second main part of the chapter deals with the motives (as an ever fundamental element of an ethical consideration) behind the process of production. It is highly likely that the main motive behind production lies in a desire to consume the produced products. Knight observes that economics has traditionally been vague on the character of economic motives, suggesting at one time the wealth-possession and other time the wealth-consumption as fundamental, but never worked out clearly the relations between these essentially contradictory incentives or between them and any other possible motives. Knight states that the motive behind production as an activity, other than the creation of a product for consumption, can best be conceptualised as a *competitive game*. Knight then raises the question that if it is really a game, then what kind of game is business? Is there anything to be said about games from an ethical point of view, any basis for judging them or ranking them as games, and if so, is business relatively good, bad, or an indifferent game? Knight interprets the features of a competitive game as being similar to the driving force of

economic life. He points out that in a system in which a want-satisfying mechanism and a competitive game exist at the same time, three ethical ideals seem to be in conflict. The first relates to distribution according to effort; the second concerns the principle of “tools for those who can use them”. The latter is a necessary condition of efficiency but involves “giving the best player the best hand, the fastest runner the benefit of the handicap”, thereby infringing the third ideal, which is to maintain the conditions of *fairness* in the game. Knight notes that any attempt to accurately formulate the conditions of a fair and interesting game leads to a difficult problem. Knight details a number of arguments in favour of distinguishing between a good competitive game and a poor one. He explains that there are three elements which affect the question of who is to win and who will therefore contribute to his own interest: these are the ability to play, effort and luck. The differences in the capacity to play the business game are extremely big from one person to another; there are handicaps but they are distributed to the advantage of the strong rather than the weak. Most likely, business ability is to some extent hereditary, and social institutions¹⁰ add to inherited personal superiority through the advantages provided by superior training, preferred conditions of entrance into the game, and an advance (inherited) distribution of the prize money.¹¹ Business in its current form does not commonly display a very high degree of sportsmanship and still the question could be raised as to whether sportsmanship itself is the highest human ideal.

The third part of Knight's observation, which he considers to be the most important in regards to the question of the ethics of competition as such, is to consider competition from the point of view of *pure ethics*. Is emulation as a motive ethically good or

9 This argument is summarised by Professor Knight in one sentence as follows: a freely competitive organisation of society tends to place every productive resource in a position in the productive system where it can make the greatest possible addition to the total social dividend as measured in price terms, and tends to reward every participant in the production process through an increased social dividend, made possible by the participants' co-operation. See Frank Hyneman Knight: *The ethics of competition*; with a new introduction by Richard Boyd, New Brunswick, N.J., USA: Transaction Publishers, 1997.

10 Here we may add that the social sector and other socially driven policies have in general been traditionally much stronger in Europe than they have ever been in the USA. The more significant role played by the state may have contributed to more balanced access and opportunities for members of society. However, the “American dream” suggests that based on your skills and effort there is no limit to your success in the USA.

11 See a notable contribution on how business ethics could contribute to society: Georges Enderle, *How Can Business Ethics Strengthen the Social Cohesion of a Society?* *Journal of Business Ethics*, Springer, first published online: 11 May 2016. 1-11., <https://link.springer.com/article/10.1007/s10551-016-3196-5>

bad? Is success in any sort of contest, as such, a noble objective? Professor Knight notes sharply that particularly in America, where competitive business and its concomitant, the sporting view of life, have reached their fullest development, two kinds of virtue have arisen: the greater virtue is to win, and the lesser virtue is to go out and die gracefully after having lost. Having earlier discussed the possibility of understanding efficiency as an element of ethical standards, Knight observes that when interpreting life in terms of power as such, including "intelligence" as a form of power, there can be little question that competitive business has been an effective tool for bringing the forces of nature under human control and has largely been responsible for the material progress of the modern era. The question remains, however, whether we are willing to accept an ethics of power as a basis of our world view.¹² After referring to the contrast between the modern scientific way of thinking and the wish for ethical consideration, Knight compares the former view against the main ethical traditions, but is unable to find any sound justification for it. As Knight observes, the Greeks were far from indifferent to recognition or glory, and the spirit of contest played a large role in the life of the people, as shown in the national games that took place. But the ideal appears to have always been the achievement of perfection, and the education of the people to recognise superior merit, not merely winning. Certainly it was not the mere winning of power. Professor Knight adds that one must hesitate to bring Christianity into scientific discussion since it has been interpreted in so many conflicting ways, but if there was anything on which divergent interpretations would have to agree, it

would be the admission that the Christian conception of goodness is the antithesis of competitive. On the contrary, it suggests that first will be last and last will be first, and whoever would be the first must be the servant of all. Professor Knight concludes by stating that the search for any real ethical basis in support of competition as a basis for an ideal type of human relations, or as a motive to action, appears to be undertaken in vain. Its only justification, as Knight summarises, is that it is effective in getting things done, but any candid answer to the question "what things" compels the admission that they leave much to be desired.

In general, we can observe that while not much attention has so far been devoted to the ethical aspects of competition law and policy in the literature,¹³ there has recently been a tendency, at least from the enforcement side, to refer to "fairness" as a central aim of competition policy. The European Commissioner for Competition, Margarethe Vestager, frequently refers to the need for fair competition¹⁴ and the European Commission's Competition Policy Annual Report (2016) seems to echo this view¹⁵. Private practitioners, however, treat this approach with moderate enthusiasm, claiming that the concept of fairness is too subjective and imprecise to be used in the day-to-day business of competition law-making and enforcement.¹⁶ While this short review does not seek to support any side of this debate, and Professor Knight's thoughts deal with a different dimension of the problem, the aim of this review is to show that detailed philosophical thinking and the desire for complex understanding do not fall outside the scope of competition related literature.

12 Professor Knight cites Fichte who said "Was für eine Philosophie man wählt hangt davon ab was für ein Mensch man ist".

13 The leading textbooks usually refer to some ethical aspect of competition law, see Richard Wish: *Versenyjog (Competition Law)* HvgOrac, Budapest, 2010. 13-14.

14 "Fairness and competition" GCLC Annual Conference, Brussels, 25 January 2018; "Competition and a fair deal for consumers online" Netherlands Authority for Consumers and Markets Fifth Anniversary Conference, The Hague, 26 April 2018; "Fair markets in a digital world" Danish Competition and Consumer Authority, Copenhagen, 9 March 2018, "State aid and fair competition worldwide" High Level Forum on State Aid Modernisation, Brussels, 28 June 2017; "Competition for a Fairer Society" 10th Annual Global Antitrust Enforcement Symposium, Georgetown, 20 September 2016; "Working together to support fair competition worldwide" UCL Jevons Institute Conference, 3 June 2016, etc.

15 Report on Competition Policy 2016, Brussels, 31.5.2017. COM(2017) 285 final.

16 Maurits Dolmans – Wanjie Lin: Fairness and competition law: A fairness paradox *Concurrences* N° 4-2017. 2.

