THE COMPETITION ASSESSMENT TOOLKIT

"Increasing productivity is by far the most important ingredient in economic development. It solves almost all other economic problems. From the vast amount of economic experience in countries all over the world for the past 50 years, we have learned without doubt that the most important condition necessary for rapid productivity growth is fair and intense competition in all the sectors of an economy."

William W. Lewis, Founding Director, McKinsey Global Institute
Author of *The Power of Productivity*

OECD

COMPETITION BRINGS PROSPERITY

1. THE TRANSFORMATIONAL POWER OF COMPETITION

Increased competition leads to better economic productivity and higher growth. A key way to strengthen competition is to eliminate any unnecessary restraints on market activities caused by laws, regulations or other government-imposed barriers. The OECD's Competition Assessment Toolkit is a practical methodology to help competition authorities and other decision-makers identify and evaluate existing and proposed policies to see whether they unduly restrict competition. Where a detrimental impact is discovered, the toolkit assists in the development of alternative ways to achieve the same objectives, with minimal harm to competition.

Competition between businesses keeps consumer prices low and promotes growth and prosperity. However government policies often restrict competition, thereby reducing its beneficial effect. Reviewing and removing unnecessary laws, regulations and other government constraints helps unleash the positive forces of competition, thereby stimulating the economy as a whole.

An excellent example of a review of government constraints occurred in Australia when it launched a broad program of comprehensive pro-competitive reforms at national and state levels in the mid-1990s. During the process it identified 1800 laws of potential concern to competition. Each was reviewed and revised, or eliminated. Since undertaking its National Competition Policy program, Australia has experienced continuous, strong economic growth that has raised it from the mid-level to one of the top performers in the OECD. The reforms have led to productivity improvements which have increased the average Australian family's annual income by 7000 Australian dollars, according to estimates by the Australian Productivity Commission. Australia's experience demonstrates the transformational power of competition.

The OECD has now developed a specific methodology to help governments eliminate barriers to competition. The Competition Assessment Toolkit is the result of this work and draws on the experiences of many OECD jurisdictions.

The toolkit can be used in four key ways:

1. As part of an overall, high-level evaluation of existing laws and regulations (either for the economy as a whole or for specific sectors);
2. As part of a Regulatory Impact Analysis process for new laws and regulations;
3. By competition authorities to structure their competition advocacy efforts; and
4. By government bodies, particularly those engaged in the development and review of policies and materials for domestic use (for example, ministries that develop laws or the competition authority when it evaluates the competitive impacts of regulations).

The toolkit is the most comprehensive guide for competition assessment available today. It can also be applied in a decentralised manner across government at both federal and state levels.

2. COMPETITION AND THE POWER OF PRODUCTIVITY

Recent analysis by the OECD's Economics Department has shown that pro-competitive policies increase productivity growth, enhance employment and promote investment. Even in countries with active market economies, increased competition delivers important positive outcomes.

Competition policy is in fact a critical factor in explaining why some countries have greater productivity – and resultant prosperity – than others. In markets where competition is weak, productivity levels are typically much lower than where competition is vigorous. This correlation applies not just to global markets, but to smaller, domestic markets as well. Furthermore, competition policies that improve productivity in particular industry sectors have been shown to have direct positive impact on the productivity of the economy as a whole.

In *The Power of Productivity*, author William Lewis compares a number of Japanese and American industry sectors and analyses why some have greater productivity than others. He draws on a study of 14 nations undertaken by the McKinsey Global Institute and concludes that competition is the key driver of productivity growth and technological advancement. He says: "Competition is the way most productive firms win out. Productivity increases as more productive firms expand and take market share away from less productive firms. Sometimes the less productive firms go out of business. Other times they react to the competitive pressure and increase their own productivity. Either way, overall productivity increases."

Government policies can weaken competition. In many sectors, laws and regulations unnecessarily restrict the entry of new competitors, limit the scope of competitive conduct and reduce incentives for active competitive engagement. When this occurs, productivity is constrained. Conversely, economic performance can be improved if governments identify and remove unnecessary restrictions on product market competition.

3. A GUIDE TO COMPETITION ASSESSMENT

Step 1 – The first step for governments and policy makers is to identify the policies, laws and regulations that may unnecessarily impede competition. At the heart of the OECD's Competition Assessment Toolkit is the Competition Checklist which has been developed to help 'filter' policy proposals, laws and regulations from a competition perspective. The checklist is designed to be used by specialists and non-specialists alike, quickly drawing their attention to areas requiring further in-depth review.

The Competition Checklist probes three kinds of government restrictions on competition:

1. Restrictions on **starting new businesses**

If existing businesses do not face the prospect of new competition, the possibility of co-operation (or collusion) between them increases. Without new competition, individual businesses may also have a greater ability to raise prices. While there may be sound policy reasons to limit the start-up of new businesses, the policy benefits of such limits need to be compared to the potentially higher prices that could follow. Examples of policies which may restrict the entry of new businesses include those that grant exclusive rights over a good or service; establish a license, permit or authorisation process as a requirement of operation; or create a geographical limit to the ability of companies to supply goods or services, invest capital or supply labour.

2. Regulations that affect the **ability of businesses to compete**

Regulations that restrict advertising and marketing, set standards that prevent competition about quality, control prices and favour particular firms or production processes are common examples. They can reduce the intensity and dimensions of rivalry, yielding higher prices for consumers and less product variety.

3. Regulations that affect business behaviour by **changing the incentive of businesses** to act as vigorous rivals.

Such regulations may facilitate co-ordination between suppliers. They may also reduce the willingness, ability or incentive of customers to switch between different suppliers. Co-ordination between suppliers over terms of competition can restrict output and raise prices, leaving consumers worse off. Examples include regulations that create a self-regulatory or co-regulatory regime; require or encourage information on business outputs, prices, sales or costs to be published; or exempt the activity of a particular industry or group of businesses from the operation of general competition law.

Step 2 – The second step is for governments and decision-makers to revise policies that unduly restrict competition.

This phase of competition assessment involves identifying the objectives of regulations, laws and policies that restrict competition; examining the rationales for these limits; and developing alternative, less restrictive means to achieve legitimate goals that promote more competition.

For most regulations, laws and policies, competition assessments are not necessary or will yield only minor benefits. Indeed in some cases, some type of restriction on competition is necessary in order to achieve government objectives. However for many others, a detailed competition assessment will indicate that there are significant benefits to be had from a revision.

Multiple options are often available for achieving a policy goal. Determining a preferred option can be a difficult task, requiring careful analysis, creativity and sector-specific knowledge. The toolkit's complete competition assessment review involves:

- **Development of feasible alternative policies** that achieve the government objective with less harm to competition;
- **Comparison of alternatives** against each other; and
- **Identification of the best option**.

A wide-ranging review can produce long-term results.

Many regulatory changes may look small, involving sectors that do not account for a large share of GDP. Yet the accumulated weight of unnecessary and unduly harmful regulation across many sectors is a major burden on productivity. When a government identifies and revises a host of policies that unduly limit competition, the aggregate effect can be very large. For this reason, a competition assessment process should not focus exclusively on "large" sectors, but also look at "small" ones across the economy.

Dramatic improvements in productivity cannot be expected to appear instantly. After the regulatory environment is improved, changing productive processes can still take time. However, over a period of years, a consistent process of competition assessment can raise productivity and living standards.

Continual evolution of the toolkit

The Competition Assessment Toolkit is currently being tested in a number of OECD member countries, including Canada, South Korea and Mexico. Canada's Competition Bureau is running a pilot program to help assess the methodology and is also developing training materials in co-operation with industry, health and other regulators. South Korea's Fair Trade Commission is using the toolkit in its own review of new government regulations, while Mexico is incorporating the toolkit into plans for a broad competition assessment review of its existing regulatory policies.

The Competition Checklist has already been incorporated into an on-going program in Australia. Other countries making significant progress towards using competition assessment are Japan and Turkey, while the European Commission has included a call for competition assessment in its development of new regulations.

Feedback from these and other countries' experiences with the toolkit will ensure that it continues to evolve in line with market developments and users' needs and expectations.

The toolkit can be downloaded from the OECD's Competition homepage: www.oecd.org/competition. It is currently available in 11 languages.

www.oecd.org/competition

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