



COMPETITION ASSESSMENT TOOLKIT

PRINCIPLES





Competition Assessment Toolkit

Volume I: Principles

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ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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FOREWORD

Increased competition improves a country's economic performance, opens business opportunities to its citizens and reduces the cost of goods and services throughout the economy. Numerous laws and regulations, however, restrict competition in the marketplace further than necessary to achieve their policy objectives. Governments can reduce unnecessary restrictions by applying the OECD's "Competition Assessment Toolkit". The Toolkit provides a general methodology for identifying unnecessary restraints and developing alternative, less restrictive policies that still achieve government objectives. One of the main elements of the Toolkit is a Competition Checklist that asks a series of simple questions to screen for laws and regulations that have the potential to unnecessarily restrain competition. This screen focuses limited government resources on the areas where competition assessment is most needed.

These materials can be used by governments in three main ways:

- In the evaluation of draft new laws and regulations (for example, through regulatory impact assessment programmes)
- In an evaluation of existing laws and regulation (in the economy as a whole or in specific sectors)
- By government bodies engaged in development and review of policies, such as ministries that develop laws or the competition authority in its evaluation of competitive impacts of regulations

The Toolkit is designed for use in a decentralised fashion across government at both national and sub-national levels. The reason for designing the materials with this flexibility is that restrictions on competition can be implemented at many different levels of government and competition assessment can be helpful at all these levels. In fact, one of the most successful examples of pro-competitive reform occurred in a federal system when Australia implemented broad, pro-competitive reforms at both national and state level in the mid-1990s. Since that time, Australia has experienced strong economic performance, with high and steady growth that has raised

Australia's economy from a mid-level performer to one of the top performing OECD economies. In a 2013 large competition assessment project, economic benefits from implementing recommended changes would amount to around EUR 5.2 billion.¹ In another, benefits were estimated at around 2.5% or more of GDP.² While not all projects will have such large impacts, benefits from competition assessment can often be substantial.

The Toolkit materials are designed for use by officials with no specialised economics or competition policy training. Institutionally, potential users could include ministries, legislatures, offices of government leaders, state governments and outside evaluators of policy. The Competition Assessment Toolkit is available in many languages in order to encourage broad use and adoption.

Competition Assessment Principles gives examples of the benefits of competition, provides an introduction to the Competition Checklist and shows some ways that governments assess competitive effects of their policies. This volume is supplemented by two companion volumes, *Competition Assessment Guidance*, which provides detailed technical guidance on key issues to consider when performing competition assessment, and the *Operational Manual for Competition Assessment*, which provides a step-by-step guide for performing competition assessment. These three volumes jointly constitute the Competition Assessment Toolkit. Further related materials can be found on the OECD's website www.oecd.org/competition/toolkit.

¹ See OECD (2014) OECD Competition Assessment Reviews: Greece. OECD, Paris.

² See Sims, R. (2013), "Driving prosperity through effective competition, speech to The Mexico Forum, 8 January 2013 Available at: [http://www.accc.gov.au/system/files/The Mexico Forum 2013 - Driving prosperity through effective competition_0.pdf](http://www.accc.gov.au/system/files/The%20Mexico%20Forum%202013%20-%20Driving%20prosperity%20through%20effective%20competition_0.pdf), and Productivity Commission (2005), Review of National Competition Policy Reforms, Inquiry Report No33.

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At the OECD Secretariat, the materials were drafted by Rex Deighton-Smith, Sean F. Ennis, Vivek Ghosal, Marta Troya-Martinez, Mark Ronayne, Cristiana Vitale and Sabine Zigelski under the leadership of Sean F. Ennis of the Competition Division. Substantial comments have been made by Peter Avery, António Gomes, Stéphane Jacobzone, Federica Maiorano, Ania Thiemann and many delegates to OECD committees. The competition assessment project is currently led by Sean F. Ennis of the Competition Division.

Marianne Aalto, Sophie Blondieau, Jenny Calder, Wendy Houet, Rebecca Lambert, Laurence Langanay, Angélique Servin and Edward Smiley contributed to the preparation of the documentation.

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CHAPTER 1.

COMPETITION ASSESSMENT AND THE COMPETITION CHECKLIST*

This chapter describes the competition checklist and its role in the competition assessment process. Readers with prior knowledge of this topic may wish to proceed directly to the technical, companion volume *Competition Assessment Guidance*.

1. Introduction

Government action routinely is designed to promote and protect important public policy goals. There usually are multiple ways to achieve these goals. Because consumers typically are better off when there is more, rather than less, competition, it is valuable to assess effects on competition when considering these options.¹ Such assessments are best performed early in the process of developing policies.

This Toolkit shows how to make that assessment. It provides a practical method for regulators and legislators to use to identify important competitive restrictions and, if possible, to avoid them. The OECD Council recommends competition assessment (see Appendix A).

The method employs, as a first step, a set of threshold questions, a “Competition Checklist,” that show when proposed laws or regulations may have significant potential to harm competition. This Checklist helps policymakers focus on potential competition issues at an early stage in the policy development process.

* This chapter has been prepared by Sean F. Ennis in conjunction with more detailed papers prepared by Rex Deighton-Smith and Vivek Ghosal.

¹ Examples of the benefits of competition are provided in Chapter 2.

While the majority of regulations do not present a risk of significant harm to competition, the competition assessment process, of which the checklist is the initial stage, provides the analytical framework regulators and legislators need to mitigate or avoid potential competition problems. It does so by aiding them in identifying possible alternatives that might reduce or eliminate potential harm to competition while continuing to achieve the desired policy objectives.

The rest of this chapter describes the four categories of questions in the Competition Checklist and first steps policymakers should take if the answer to any of those questions is “yes.” It also gives some first ideas for potential policy alternatives to be considered.

2. Are there limits on the number or range of suppliers? (Checklist A)

Limiting the number of suppliers leads to the risk that market power² will be created and competitive rivalry will be reduced. When the number of suppliers declines, the possibility of diminished competition (or collusion) among the remaining suppliers increases, and the ability of individual suppliers to raise prices can be increased. The resulting decline in rivalry can reduce incentives to meet consumer demands effectively and can reduce innovation and long-term economic efficiency. While there are sound policy reasons why policy makers may sometimes limit the number or range of suppliers, as discussed below, the policy benefits of entry limits need to be carefully balanced against the fact that ease of entry by new suppliers can help prevent existing suppliers from exercising market power or colluding.

² Market power of suppliers is the ability to profitably increase price, decrease quality, or decrease innovation relative to the levels that would prevail in a competitive market.

Competition Checklist

Further competition assessment should be conducted if the proposal has any of the following 4 effects:

(A) Limits the number or range of suppliers

This is likely to be the case if the proposal:

- 1 Grants exclusive rights for a supplier to provide goods or services
- 2 Establishes a license, permit or authorisation process as a requirement of operation
- 3 Limits the ability of some types of suppliers to provide a good or service
- 4 Significantly raises cost of entry or exit by a supplier
- 5 Creates a geographical barrier to the ability of companies to supply goods services or labour, or invest capital

(B) Limits the ability of suppliers to compete

This is likely to be the case if the proposal:

- 1 Limits sellers' ability to set the prices for goods or services
- 2 Limits freedom of suppliers to advertise or market their goods or services
- 3 Sets standards for product quality that provide an advantage to some suppliers over others or that are above the level that some well-informed customers would choose
- 4 Significantly raises costs of production for some suppliers relative to others (especially by treating incumbents differently from new entrants)

(C) Reduces the incentive of suppliers to compete

This may be the case if the proposal:

- 1 Creates a self-regulatory or co-regulatory regime
- 2 Requires or encourages information on supplier outputs, prices, sales or costs to be published
- 3 Exempts the activity of a particular industry or group of suppliers from the operation of general competition law

(D) Limits the choices and information available to customers

This may be the case if the proposal:

- 1 Limits the ability of consumers to decide from whom they purchase
- 2 Reduces mobility of customers between suppliers of goods or services by increasing the explicit or implicit costs of changing suppliers
- 3 Fundamentally changes information required by buyers to shop effectively

2.1. *Grants of exclusive rights (Checklist A1)*

A grant of an exclusive right to produce a certain good or provide a certain service represents the establishment of a private monopoly. Historically, the grant of an exclusive right frequently occurred in the context of a “natural monopoly”.³ The grant of exclusive rights, particularly if given for a long duration, has frequently been considered a means of encouraging substantial investments in infrastructure that may be unlikely to occur without the incentives provided by the guaranteed market the grant of an exclusive right provides. But exclusive rights are sometimes used in situations where the natural monopoly justification for them does not apply.

Exclusive rights are in many respects the ultimate entry barrier. Exclusive rights are likely to yield monopoly pricing and other problems associated with the exercise of market power. Such results may not be fully avoided through regulation because regulators often fail or achieve only a low level of success in preventing the exercise of market power and protecting consumers. Therefore, such rights should be limited and established only after careful consideration of prices to be charged, duration of the rights and alternative ways to achieve the same objectives.

Alternative policy options

If there are no other alternatives, regulators may wish to consider auctioning the exclusive right. Advice should be sought from government or other economists as to the type of auction that will be most appropriate for the proposed sale of rights. Where such a right is granted, particular attention needs to be paid to regulatory design. For example, issues need to be addressed such as the relative appropriateness of “cost-plus” pricing regulation versus “rate-of-return regulation” versus “price-cap” regulation. Moreover, in many cases, the splitting of the exclusive right between two or three parties can conserve competitive dynamics to some degree while still reaping the benefits sought.

2.2. *License or permit requirements (Checklist A2)*

Licenses or permits required for operation necessarily restrict entry. Qualifications requirements can take the form of minimum standards for formal education and/or experience and may include good character requirements. For example, so-called “fit-and-proper” tests are commonplace in finance for participation in an official capacity at company and board levels. At times, a “public

³ A monopoly exists when a good or service can reasonably be purchased only from one supplier. In a “natural monopoly”, one supplier can produce desired output more efficiently and at a lower total cost than two or more suppliers.

interest” test may be applied that requires that potential entrants demonstrate the “need” for an additional service to be provided and, in some cases, even if their entry would have no negative impact on the businesses of existing industry participants. In extreme cases, there may be fixed numbers of licensees.

License or permit requirements are often stricter than is necessary for consumer protection and can unnecessarily reduce consumer choice and create artificial scarcity that raises prices. While licensing schemes often have well-founded consumer protection objectives, such barriers frequently have the effect of protecting incumbent producers from competition. Care needs to be taken that license and permit requirements do not become more onerous than is necessary to achieve the sought regulatory objectives.

Alternative policy options

Product quality standards should be set no higher than necessary to ensure consumer safety. Likewise, restrictions on supplier size (e.g., no more than one storefront per professional) should not be set at levels that create substantial anti-competitive impacts or inefficiencies. Similarly, when considering the need for compulsory insurance requirements, performance bonds and the like, consideration should be given to the nature and extent of the consumer harms that can potentially result from either poor practice or from the failure of a service provider. How well consumers will be at informing themselves of potential harms and protecting themselves by making informed choices of providers is an important consideration, as is whether alternative approaches that would enhance consumer knowledge in this area are viable.

2.3. *Limits the ability of some types of suppliers to provide a good or service (Checklist A3)*

At times, governments limit the ability of other types of suppliers to participate in a business activity. For example, some governments require that all real estate brokers provide a government-mandated set of services, and thus limit or prohibit provision of services by low-cost minimum-service brokers, or fee-for-service brokers.⁴ Such restrictions are often excessive because they unduly restrict the number of suppliers, reduce competition between suppliers and result in higher prices or less desirable contract terms for customers.

⁴ See http://www.usdoj.gov/atr/public/real_estate/feeforservice.htm.

Alternative policy options

Where regional or small business policy objectives are sought, alternatives less deleterious to competition may include a range of direct subsidies and/or tax benefits, more favourable regulatory provisions for the small or regional provider, or the use of publicity/educational campaigns.

2.4. *Significantly raises the costs of entry or exit (Checklist A4)*

Regulations that raise the costs of entry to, or exit from, a market will tend to discourage some potential entrants and so reduce the number of participants in the market over time. Examples of this kind of regulation include rigorous product testing requirements and requirements to meet unnecessarily high educational or technical qualifications.

Alternative policy options

Governments have sometimes acted to minimise the competitive impacts of such provisions by providing targeted exemptions. For example, low-volume car manufacturers are often exempted from aspects of vehicle testing regulations, or subject to less onerous testing protocols. In some circumstances alternatives such as greater information provision or product disclosure requirements can be considered in order to enable more informed consumer choice. In other cases, regulation may be required even though it raises entry costs and the focus should be on minimising anti-competitive potential by ensuring that the requirements set are the minimum necessary to achieve an adequate degree of consumer protection.

2.5. *Restricts the geographic flow of goods, services, capital and labour (Checklist A5)*

Regulations sometimes limit the flow of goods, services, capital and/or labour across jurisdictional boundaries, often as an instrument of regional policy. Such limitations, however, artificially reduce the geographic area of competition for provision of a good or service. This may reduce the number of suppliers and potentially allow suppliers to exercise market power and increase prices.

Potential restrictions should be assessed based on whether there is a clear link between the restrictions and the achievement of specific policy goals, whether the restrictions are the minimum necessary for achievement of the goal, whether a reasoned analysis suggests the policy goal will be achieved by means of the restriction and whether the restrictions are limited to a finite time span via explicit regulatory provisions.

There is a substantial risk that “temporary” protections will develop into quasi-permanent arrangements as a result of substantial lobbying by the suppliers that benefit from the restrictions.

Alternative policy options

There will often be superior alternatives available to achieve the regulatory objective, including direct subsidies and favourable regulatory treatment. In general, there are relatively few contexts in which such restrictions are likely to pass a benefit/cost test. Therefore, policymakers should adopt a generally sceptical view of proposed regulation that includes such restrictions.

3. Are there limits on the ability of suppliers to compete? (Checklist B)

Regulation can affect the ability of suppliers to compete in a variety of ways, not all of which are identified here, including through advertising and marketing restrictions, setting of standards for product or service quality, and controls over prices at which goods or services are sold. These limits can reduce the intensity and dimensions of rivalry, yielding higher prices for consumers and less product variety.

3.1. Controls the prices at which goods or services are sold (Checklist B1)

Governments often regulate prices in traditional monopoly sectors, such as utilities. These types of price controls are probably helpful to consumers and serve as a counterweight to a lack of consumer alternatives. However, price controls are also sometimes applied in situations where there are many potential suppliers to the same consumer. When minimum prices are set, low-cost suppliers are prevented from winning market share by providing better value to consumers. Similarly, when maximum prices are set, supplier incentives to innovate by providing new and/or high-quality products can be substantially reduced, and suppliers may effectively co-ordinate their prices around the maximum price.

Minimum price regulation is sometimes a response to extremely vigorous price competition. In these cases, minimum price regulation is generally seen as a means of protecting small suppliers from “unfair” competition. The impacts of such price regulations merit careful evaluation because the result is likely to be higher prices for consumers or unmet demand. Maximum price regulations are frequently introduced as a necessary corollary to restrictions on entry. An alternative is to permit freer entry to the market.

Alternative policy options

Price regulation rarely constitutes the most effective or efficient means of achieving the intended objectives. For example, in the case of the taxi market, a better means of protecting consumers is to address the restrictions on supply in the market. In the case of “predatory pricing” concerns, the use of the general competition law is likely to be a superior alternative. Thus, regulation proposing to control prices should be subject to especially rigorous scrutiny.

3.2. *Restricts advertising and marketing (Checklist B2)*

Regulations that restrict suppliers’ ability to advertise or market goods and services often exist to limit false or misleading advertising. Sometimes advertising restrictions are intended to reduce advertising for products or services that are deemed to have a socially negative value or that are subject to excess consumption. At other times, advertising to certain “vulnerable” groups, such as children, may be restricted. Restrictions of this nature, when circumscribed to ensure they are not overly broad, can have significant social benefits.

In many cases, however, advertising and marketing restrictions are too broad and unduly restrict competition. Restrictions on advertising and marketing are likely to be particularly onerous for potential entrants, as they restrict an entrant’s ability to inform potential customers of their presence in the market and of the nature and quality of the goods and services that they are able to offer.

Alternative policy options

General consumer protection laws almost invariably contain prohibitions on misleading and deceptive advertising practices. These promote efficient markets and are effectively pro-competitive and usually obviate the need for any further, product- or service-specific advertising restrictions. Where there is a need to discourage over-consumption, alternative approaches to advertising restrictions include information campaigns and consumption taxes. These constitute more direct, effective, means of addressing the identified policy issue.

3.3. *Sets standards for product quality that provide an undue advantage to some suppliers over others or that are above the level that some well informed customers would choose (Checklist B3)*

Regulations setting standards often provide benefits to consumers and can help to promote new types of products by ensuring that new products from different suppliers are compatible. But standard setting can also provide undue advantages to

some suppliers over others. One common example is environmental regulations that limit the allowable emissions of a mildly toxic substance. While limiting emissions is often appropriate to protect public health, regulations can be designed in ways that unfairly advantage a small number of suppliers, for instance by requiring a particular technology or by setting unduly strict standards that are difficult or impossible for less well resourced producers to meet. Another example in which standard-setting can have a significant anti-competitive impact is where minimum quality standards are set for particular product types. There are often sound objectives underlying such standard-setting, such as protection of consumers from risks associated with the use of the product. However, when some consumers prefer lower cost over increased safety, the need for the standard is less clear. Consumer welfare can be reduced by such standards as consumers are prevented from buying cheaper, lower quality goods that they would prefer, even when fully informed of all associated risks.

Alternative policy options

Alternatives often exist to stricter product standards regulations. For example, when minimum standards are pursued for consumer protection reasons, it may instead be possible to require disclosure of certain product characteristics. Where major changes in emissions standards are contemplated, governments can seek to minimise anti-competitive impact by permitting trading of emission rights or providing temporary assistance to smaller suppliers in order to help them meet the new requirements.

3.4. *Raises the costs of some suppliers relative to others (Checklist B4)*

At times, regulations have the effect of raising costs for some suppliers relative to others. One source of cost asymmetry is regulations that unnecessarily require the use of one technology of production over another. Another source is “grandfather clauses” that exempt current suppliers from a regulation but apply the regulation to new entrants. Another source is subsidies or preferential financing for state owned enterprises. Such arrangements have substantial potential to distort competitive relations within the industry by influencing the costs to some suppliers to a substantially greater extent than to others. This can create inefficiency, impede entry, reduce corporate-led innovation and lower the intensity of competitive pressure in the market. While creating cost differentials can be harmful, that is not to say that regulations should affirmatively seek uniform supplier costs.

For occupational qualifications, grandfather clauses are often implemented based on the belief that extensive practical experience of long established practitioners is an adequate substitute for a higher level of formal qualification. In

relation to productive technologies, grandfather clauses are often implemented to ensure adequate time exists to amortise the sunk costs of previous investments.

Alternative policy options

The anti-competitive impact of grandfather clauses can be minimised by ensuring that they are time-limited, rather than permanent, and that the duration of the exemption given is strictly proportionate to the underlying rationale for its being granted in the first place. More generally, however, a sceptical approach needs to be taken to arguments in favour of the need for grandfather clauses, as they are frequently a reflection of attempts to defend vested interests from potential competition.

Subsidies can provide benefits in many circumstances; but when they fundamentally alter terms of competition by providing advantages to firms that are inefficient, they may move business to less efficient providers. Alternatives to subsidies can include restructuring to eliminate uneconomic activities and to make businesses run with higher productivity, though at times special subsidies may be required to support such restructuring. In some jurisdictions, limits are placed on subsidies to ensure they are not ongoing, that they are genuinely aimed at improving performance of viable companies and address market failures, and that their negative effects on competition remain limited.

**4. Are there reductions in the incentives for suppliers to compete?
(Checklist C)**

Regulations can affect supplier behaviour not only by changing the suppliers' ability to compete but also by changing the incentive of suppliers to act as vigorous rivals. Two of the main reasons why suppliers may compete less vigorously are first, that some regulations may have the effect of facilitating co-ordination between suppliers and, second, that some regulations may have the effect of reducing the willingness, ability or incentive of customers to switch between different suppliers. Other reasons suppliers may compete less vigorously exist, such as profit or market share limits that restrict the potential reward from competing. Cartel-like behaviour⁵ may be more readily generated under self-regulatory or co-regulatory regimes, by increasing the sharing of supplier output and price information or by excluding an industry or sector from the reach of competition law. Cartels are harmful because

⁵ A cartel exists when competitors make an agreement to restrict competition, for example by setting a price, limiting supply, sharing profits or rigging bids, thus increasing their collective profits.

they restrict output and raise prices, making consumers worse off. The risks of cartel activity must be balanced against potential benefits of self-regulation, such as quicker certification of new technologies.

4.1. *Self-regulation and Co-regulation (Checklist C1)*

When an industry or professional association takes full responsibility for regulating the conduct of its members, without government legislative backing (often at the urging of government) the term “self-regulation” is used. However, when government provides legislative backing to rules that are developed at least in part by the industry/professional association, the term “co-regulation” is used. Self-regulatory and co-regulatory structures can yield substantial benefits by ensuring that technical standards are appropriate and that standards advance with technology.

However, these structures can have significant anti-competitive impacts. In particular, industry/professional associations often adopt rules that reduce incentives or opportunities for vigorous competition between suppliers of goods or services, such as advertising restrictions and rules that prevent discounting. In addition, unduly strict qualifications requirements may reduce entry to the market.

Alternative policy options

Government should retain powers to prevent attempts by the industry/professional association to use regulatory powers in an anti-competitive manner. This may include ensuring either that the self-regulation or co-regulation should clearly remain subject to competition law enforcement, or that the relevant governmental authorities have the right to approve, or refuse to approve, association rules and, as required, to substitute their own should the association continue to propose unacceptable rules.

4.2. *Requirements to publish information on supplier prices, outputs or sales (Checklist C2)*

Regulations that require market participants to publish information on their prices or output levels can significantly assist in the formation of cartels, since a key requirement for cartel operation is that participants in the cartel can effectively monitor their competitors’ (or co-conspirators’) market behaviour. Cartels and tacit co-ordination are more likely to arise where there are fewer participants in the market, where entry barriers are high, where suppliers’ products are relatively homogeneous and where information about price or output changes is available either before or soon after the price or output changes.

Regulations requiring the publication of information such as price and output levels may be adopted to improve consumer information and, at times, can improve the efficiency of markets. However, when cartel formation is likely, such requirements are more likely to have a net negative impact. Alternatives exist to publishing all collected data.

Alternative policy options

When the information is gathered primarily for government policy making, there may be no need to publish it at all. When the purpose is to aid consumers or provide general statistics, aggregate statistics are less supportive of cartels than company-specific statistics, and historical statistics are less supportive than contemporaneous information. Statistics aggregated across companies will not help cartel members to identify a supplier that is violating the cartel agreement, while company-specific statistics could clearly identify a company that deviated from a cartel agreement over pricing or quantity. Historical statistics provide less useful information for cartels because cartels often need to share current information to decide how to allocate output and set price targets, and historical information would not help them substantially in this task.

4.3. Exemptions from general competition laws (Checklist C3)

In many countries, particular suppliers or economic sectors benefit from exemptions from the general competition law. In some cases, these sectors are subject to their own, sector-specific competition laws. In other cases, no restrictions exist on anti-competitive conduct in these sectors. Where a substantial derogation from the general application of competition law exists there is a clear risk of cartels, pricing abuses and anti-competitive mergers⁶.

Alternative policy options

Where a specific rationale for the continued existence of exemptions has been identified, consideration should be given to the means by which their scope can be minimised. For example, a legislated monopoly requiring all producers of a particular commodity to sell to a licensed intermediary may be inferior to a system that allows producers to engage in co-operative selling arrangements, but does not compel them to do so.

⁶ A merger is a combination of two (or more) previously independent firms to form one larger firm.

5. Are there limits on the choices and information available to customers? (Checklist D)

5.1. *Limits on ability of consumers to decide from whom they purchase goods or services (Checklist D1)*

Regulations sometimes limit the choices available to consumers. For example, a regulation may restrict customers to purchasing medical services locally. Such a regulation could limit quality of care and prevent those consumers who would be interested in travelling (for example, to a clinic with shorter waiting lists or a better reputation) from doing so.

Limits on consumer choice can be harmful, because the suppliers who remain can have less incentive to satisfy consumers by delivering products of desired quality and price.

Alternative policy options

Perhaps the most natural alternative is better information. But often the existence of a restriction means information is simply not enough. In the case of contact lens prescriptions, the prescription rules were modified so that prescribers who issued a prescription with a private label contact lens had to provide sufficient information so that close alternatives on the market could be identified and legally substituted by contact lens sellers. (For more details, see Section 4.4.1 of the Competition Assessment Guidance, volume II of the Competition Assessment Toolkit.)

5.2. *Reduces the mobility of customers by increasing the costs of changing suppliers (Checklist D2)*

Regulations can make consumers more or less willing to switch suppliers by affecting “switching costs” – the explicit and implicit costs borne by a consumer in changing from one supplier to another. Switching costs may arise for various reasons, including long contract terms or tying of assets to suppliers in a way that makes switching inconvenient, as with tying a phone number to a given service provider. When consumers face high switching costs, suppliers can charge higher prices for their goods or services. Suppliers therefore often seek to create high switching costs, sometimes by promoting policies that will ensure high switching costs.

Alternative policy options

The pro-competitive impact of reducing or eliminating switching costs can be large, and policymakers should seek to avoid policies that raise switching costs for

consumers. Where there is a clear risk of switching costs being imposed, the inclusion of provisions in the regulatory structure that will limit or prohibit their use may be advisable. Due care should be taken to ensure that legitimate costs of consumer switching are considered. Even where the supplier is required to incur substantial costs as a consequence of the switching process, it still may be that the pro-competitive impact of reducing or eliminating the switching costs is sufficiently large that the regulator will wish to prevent suppliers from explicitly recovering those costs from consumers. Competition between businesses prior to a customer purchase decision may help to lower negative impacts from switching costs.

5.3. *Fundamentally changes information required by buyers to shop effectively (Checklist D3)*

When governments deregulate, and introduce markets that have not previously existed, consumers will be asked to make choices between products for which they have never previously shopped. One example in which this occurs is with consumer purchases of electricity. When consumers are given the right to select their supplier in new markets, it can be more difficult for them to evaluate offers and distinguish good companies from bad ones. A danger that can follow from such situations, absent an information requirement due to the “new” nature of the product, is that the reforms will be rolled back due to consumer complaints about companies that take advantage of consumer inexperience.

Alternative policy options

To ensure the deregulation survives and is considered a success, it may be better to accompany the creation of new choices with an information requirement that provides consumers with a reference point for comparing offers.

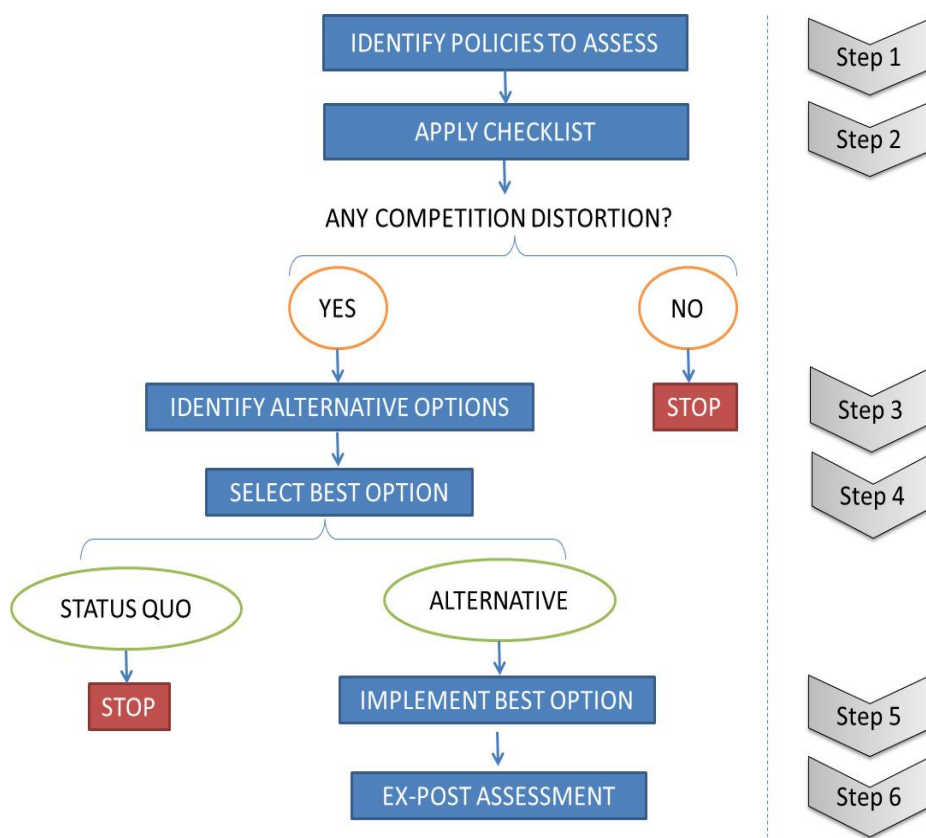
Alternatives to such information requirements include government run information and educational programmes. These may distribute leaflets or public service television commercials to help educate consumers about the choices they will have to make after deregulation.

6. When the answer is “yes”

Identifying regulations that may unduly restrict competition is the important first step for improving the quality of regulation. The questions listed on the Competition Checklist provide a reliable initial basis for identifying regulations that may give rise to an anti-competitive impact. The sub-points under the questions indicate the main, but not exclusive, ways in which regulations may unduly restrict market rivalry.

With the Checklist, only a minority of regulations will likely be found to have the potential to unduly constrain market activity. When, however, the Checklist suggests that there is a potentially excessive constraint on market activity, performing a more comprehensive competition assessment merits consideration. Chapter 3 discusses how to fit competition assessment into governmental operations. The *Operational Manual* describes how to do such an assessment.

Figure 1. Steps in Competition Assessment



CHAPTER 2

HOW COMPETITION BENEFITS CONSUMERS* AND POSITIVELY AFFECTS PRODUCTIVITY, GROWTH, INNOVATION AND EMPLOYMENT

This chapter provides examples of how competition delivers substantial benefits to consumers. It also summarises the main beneficial effects on macro-economic outcomes such as productivity, growth, innovation, employment and inequality.¹

1. Consumer Benefits

An important reason for market reforms is that governments are clearly recognising the benefits of competition.² The Competition Assessment Toolkit focuses on providing practical tools for governments to limit excessive restrictions on competition. Prior to using such tools, it is worth considering why increased competition between businesses is a goal worth pursuing.

Competition among businesses can deliver improvements in production efficiency and bring newer and better products to consumers through innovation, leading to gains in economic growth and consumer welfare. Broadly speaking, competition between suppliers generally leads to lower prices and greater choice. One of the best ways to understand these benefits that go directly to consumers is

* The examples in this chapter were prepared by John Davies, Vivek Ghosal, and Cristiana Vitale.

¹ Based on the OECD Factsheet on how competition policy affects macro-economic outcomes; OECD October 2014.

² In many of the de-regulated industries such as telecommunications, electricity and airlines, one of the benefits of competition that was touted was that it would eventually reduce excess capacity that had been built under regulation, leading to greater efficiency in production and lower prices for consumers. Muris (2002) points to the fact that since many industries are being privatised or liberalised across the world, governments are clearly recognising the benefits of competition.

through examples. Selected examples are presented in Box 1. These examples are meant to illustrate the overall benefits of competition, without necessarily focusing on regulatory restrictions.

Box 1. Examples of Benefits to Consumers from Competition

1. Shipping Ports.

Argentina started privatising some seaport services in the 1970s. This phase of privatisation did not have much success in terms of productivity. Public investments in infrastructure remained low, the system was over-regulated and port institutions were inadequate. In the 1990s, private firms were allowed to operate public ports and to build new ports or invest in their infrastructure. In the case of the port of Buenos Aires, its six terminals were given in concessions to five different private firms, while the Port Authority retained the ownership of infrastructure (landlord port model). As a result of the reforms, cargo handling increased by 50% between 1990 and 1995, labour productivity surged by 275% and Argentinean ports became the cheapest ports in Latin America. In 1997, Puerto Nuevo's cargo handling surpassed that of Santos (Brazil), the biggest port in South America. Foreign firms participated in the construction of new ports, as in the case of a terminal in Zarate.

Sources:

Lourdes Trujillo and Tomás Serebrisky. "An Assessment of Port Reform in Argentina: Outcomes and Challenges Ahead," World Bank, 2004. http://www.worldbank.org/wbi/regulation-f/pdfs/portreform_argentina.pdf

"Infrastructure in Trade and Economic Development," World Trade Report, World Trade Organization, 2004. http://www.wto.org/English/res_e/booksp_e/anrep_e/wtr04_2b_e.pdf

2. Retail Stores.

The effects of increased competition in grocery and other retail stores have been noted in several studies. For the U.S. markets, Hausman and Liebttag note that when Wal-Mart originally enters a market, its prices are between 10% and 25% lower for the same products compared with large retail chains such as Kroger, Publix, Target, and others. After Wal-Mart opened a store near a Kroger supermarket in Houston, sales at the Kroger dropped 10% even though its prices declined after the arrival of new competition. This effect indicates that consumers benefited from Wal-Mart's entry. Other benefits of competition that have been associated with the appearance of grocery superstores include: (a) new products and greater variety in the stores; (b) store renovation with wider aisles, better lighting and arrangement of products; (c) increase in the number of check-out counters. Efforts to prevent such stores from opening through regulation would prevent the achievement of the price and quality benefits to consumers.

Sources:

Jerry Hausman and Ephraim Leibtag. "Consumer Benefits from Increased Competition in Shopping Outlets: Measuring the Effect of Wal-Mart." <http://econ-www.mit.edu/files/1765>

"Wal-Mart Throws an Undercut at Target." *The Washington Post*, December 16, 2005. <http://www.washingtonpost.com/wp-dyn/content/article/2005/12/15/AR2005121502096.html>

3. Railways.

Lalive and Schmutzler (2007) study the effects of introducing competition for local passenger railway markets in the German state of Baden-Württemberg (one of Germany's largest states) over the period 1994 to 2004. They find that while DB Regio was still the dominant operator ten years after the reforms were introduced, its competitors, the NE-operators, expanded their market share from about 3% at the beginning of the reform to 13.2% in 2004. They find that the frequency of service in Baden-Württemberg increased substantially from 1994 to 2004 and that the frequency of service on those lines that were procured competitively developed more favourably than on those that were not. They find: (1) a 29% increase in total transportation; (2) a much stronger increase in the competitive group (45% vs. 22% in the control group); and (3) an increase from 19 to 39 in the number of lines operated at least partly by competitors of DB Regio. Overall, one can conclude that injecting more competition resulted in greater quantity (frequency of service) as well as an increase in convenience for consumers that the higher frequency brings.

Source:

Rafael Lalive and Armin Schmutzler. "Exploring the Effects of Competition for Railway Markets," University of Zürich, February 2007. <http://ideas.repec.org/p/soz/wpaper/0511.html>

4. Road Transport.

There is evidence about employment effects in France from changes to road freight transport regulations. In France, former prime minister Balladur's government eliminated a previously existing requirement that a government-issued license was needed to transport merchandise more than 150km. After the reform, prices for road transport fell and margins fell, suggesting that there had been high rents in the sector. In terms of employment in the sector, employment had been growing at a rate of 1-1.5% per year prior to the reform. During the years after the reform, employment grew at 5% and now grows around 4% per year. There were strikes (1992, 1995) because of the reform and how it was implemented. But, according to Cahuc and Kamarz (2005), the net effect was the creation of jobs.

Sources:

OECD. "Draft Summary of the Discussion of the Round Table on Competition and Regulation in the Legal Profession." Working Party No. 2 on Competition and Regulation, October 2007. (See comments of Francis Kramarz, p.16)

Cahuc, Pierre, and Francis Kramarz. "De la Précarité à la Mobilité: vers une Sécurité Sociale Professionnelle," Report to the Minister of Economics and the Minister of Labor, June 2005, La Documentation Française, Paris.

<http://www.ladocumentationfrancaise.fr/rapports-publics/054000092/index.shtml>

5. Automotive Parts.

Warren-Boulton and Daniel Haar (2007) provide estimates of the amount of economic benefits to consumers from competition in the market for automotive collision parts. They show that consumers benefit in two ways when Keystone (or another seller of competitive parts) enters the market with a competitive alternative to an Original Equipment Manufacturer (OEM) part. They consider two effects: (a) Keystone's price will typically be lower than the OEM's price; and (b) Keystone's entry and competition typically results in the OEM reducing

its price. Their calculations show that on average: (a) Keystone's automotive part prices are about 26% lower than the prices of the OEM parts they compete against; and (b) prices of OEM parts were reduced by about 8% due to this competition. Regulations that require the use of OEM parts can harm consumers.

Source:

Frederick R. Warren-Boulton and Daniel E. Haar. "Estimation of Benefits to Consumers from Competition in the Market for Automotive Parts." Microeconomic Consulting & Research Associates, Inc., 2007. <http://www.qualitypartscoalition.com/pdfs/8-2micraanalysisl.pdf>

6. Book Publishing.

The Net Book Agreement (NBA) which existed before 1997, prevented booksellers in the UK and Ireland from selling below the publisher's chosen price. After the NBA was abolished, a basket of best-selling books was, on average, discounted by 28 percent. Just after the NBA was abolished, 41 percent of books were discounted. Six years later in 2006, 52 percent of books were discounted. Other benefits included, for example: (a) growth of new book titles published increased from an average of 3 percent per year to over 4 percent; (b) expanded selection in stores and improved customer service.

Source:

"The Benefits from Competition: Some Illustrative UK Cases." <http://www.berr.gov.uk/files/file13299.pdf>

7. Housing.

Atterhög (2005) uses data to explore the effects on rents and quality of housing services of the privatisation of apartments by municipal housing companies located outside metropolitan areas in Sweden. He finds that: (a) in several markets, more competition led to lower rents, with the decreases being in the 2%-5% range; and (b) on average, there was no significant change in the quality of housing services due to privatisation. The results on the quality of apartments varied across specific-owners.

Source:

Atterhög, Mikael. "Increased Competition in the Swedish Housing Market and Its Effect on Rents and Quality of Housing Services for Households," *Housing, Theory and Society*, Vol. 22, No. 1, 32-49, 2005. <http://www.ingentaconnect.com/content/routledg/shou/2005/00000022/00000001/art00003>

8. Stock Exchange.

The monopoly stock market operator the Australian Securities Exchange started offering stockbrokers fee discounts under the threat of competition from two overseas rivals – Liquidnet and AXE – which planned to set up operations in Australia. Liquidnet was and is US-listed and AXE ECN was backed by the New Zealand Exchange and major brokerage houses Citigroup, CommSec, Goldman Sachs JBWere, Macquarie and Merrill Lynch. AXE and Liquidnet were promoting alternative trading systems for market crossings, or off-market trades between fund managers, which accounted for about 30 per cent of all equity trades.

Source:

"Exchange cuts fees as competitors lurk." *The West Australian*, August 25, 2007. <http://www.thewest.com.au/default.aspx?MenuID=33&ContentID=38376>

9. Airlines.

Prior to the 1990s, the EU aviation market was heavily regulated in terms of airlines' access to routes and prices. Agreements between member states restricted access to markets and often allowed only one airline to operate a service on a limited number of specified routes. During the 1990s, domestic markets were opened up and eventually became free to competition from all EU-licensed carriers. Low-cost airlines emerged as a result of greater opportunities for competition. Some of the results of the increased competition were: (a) traditional carriers began to offer services such as online booking and pricing simplicity to compete with the low-cost carriers. The simplified fare structure gives lower fares, greater flexibility, and more choice to customers. For example, advance purchase and Saturday night stay restrictions were removed; (b) price decreases were considerable. EU carriers' average lowest non-sale fares had fallen by 75% in nominal terms; (c) European flight frequency increased by 78%. Over the period, domestic flight frequency more than doubled; and (d) there was an increase in service variety. The average number of airlines operating on sample routes increased from 3 to 4 between 1992 and 1997, and further increased in 2003.

Source:

www.berr.gov.uk/files/file13299.pdf

10. Telecommunications.

"The French Consumer organisation UFC Que Choisir has stated that the least expensive SIM-only offers in the French market, offered by the low-cost Internet brands of the incumbent operators, before Free Mobile entered the market, were between USD 46.6 and USD 54.7 per month (EUR 34 and EUR 39.90), with either 2 hours or unlimited calls and 1-2Gbyte of data. Following its entry into the market, Free Mobile offered unlimited calls and 3GByte of data for US 27.4 (EUR 19.99) per month. It should also be noted that these low-cost brands had started in anticipation of the arrival of Free."

Source:

OECD (2014), "Wireless Market Structures and Network Sharing", OECD Digital Economy Papers, No. 243, OECD Publishing. <http://dx.doi.org/10.1787/5jxt46dzl9r2-en>

2. Positive Effects on Macro-Economic Outcomes

When customers can choose between different providers, they benefit and so does the economy as a whole. Their ability to choose forces firms to compete with one another. Choice for customers is a good thing in itself, but competition between firms also leads to increased productivity³ and economic growth.

³ Unless specified the term productivity refers to total factor productivity.

It can be hard directly to measure the effect of – for example – competition law on economic growth. But there is solid evidence in support of each of the relationships shown below.⁴



Most importantly, it is clear that industries where there is greater competition experience faster productivity growth. This has been confirmed in a wide variety of empirical studies, on an industry-by-industry, or even firm-by-firm, basis. This finding is not confined to “Western” economies, but emerges from studies of the Japanese and South Korean experiences, as well as from developing countries.

The effects of stronger competition can be felt in sectors other than those in which the competition occurs. In particular, vigorous competition in upstream sectors can ‘cascade’ to improve productivity and employment in downstream sectors and so through the economy more widely.

The main reason seems to be that competition leads to an improvement in allocative efficiency by allowing more efficient firms to enter and gain market share, at the expense of less efficient firms. Regulations, or anti-competitive behaviour preventing entry and expansion, may therefore be particularly damaging for economic growth. Competition also improves the productive efficiency of firms, as firms facing competition seem to be better managed. This can even apply in sectors with important

⁴ A detailed overview of literature and studies proving this point is given in the OECD Factsheet on how competition policy affects macro-economic outcomes.

social as well as economic outcomes: for example, there is increasing evidence that competition in the provision of healthcare can improve quality outcomes.

There is also evidence that intervening to promote competition will increase innovation. Firms facing competitive rivals innovate more than monopolies. The relationship is not simple: it is possible that moderately competitive markets innovate the most, with both monopoly and highly competitive markets showing weaker innovation. However, as competition policy does not focus on making moderately competitive markets hyper-competitive, but rather on introducing or strengthening competition in markets where it does not work well, this would still imply that most competition policies serve to promote innovation.

Because more competitive markets result in higher productivity growth, policies that lead to markets operating more competitively, such as enforcement of competition law and removal of regulations that hinder competition, will result in faster economic growth.

The evidence base regarding product market deregulation is stronger still, because there have been many different deregulation events, allowing comparison between industries, between countries and over time. Furthermore, regulatory policies specifically designed to introduce and promote competition – especially in network industries – have resulted in productivity gains.

Of course there are policy objectives other than GDP growth, and the OECD has been a vigorous champion of measuring such objectives more rigorously, and taking them better into account when formulating policy. The effect of competition on **inequality** has been little studied, and is often assumed to be malign as competition creates winners and losers. However, restricting competition causes harm to the many, while the profits generally go to the few. The poorest in society are often the worst affected by higher prices or lower quality and choice resulting from restrictions on competition.

Similarly, there is often a gap between reality and perceptions when **employment** concerns are prominent. It is true that the productivity gains caused by competition can result in layoffs, but this is no more likely to add to unemployment in aggregate than any other form of technical progress. Ensuring that investment in new and productive alternative means of employment then becomes key. Furthermore, restrictions on competition have been shown to reduce output and employment.

Introducing more competition and opening markets up to competition through a thorough competition assessment of new or existing laws and regulations will thus significantly contribute to economic growth, increased productivity and higher overall welfare.

CHAPTER 3

FITTING COMPETITION ASSESSMENT INTO GOVERNMENT OPERATIONS*

This chapter discusses how competition assessment can be effectively incorporated into government activities.

1. Introduction

As we have seen, competition assessment is the process of evaluating government regulations, rules and/or laws to (1) identify those that may unnecessarily impede competition and (2) redesign the identified ones so that competition is not unduly inhibited. Effectively fitting this process into government operations and institutions realistically requires consideration of the following five topics:

- Which policies merit a competition assessment?
- When should a competition assessment be performed in the policy development process?
- Who should be responsible for drafting and reviewing a competition assessment?
- How can policymakers without responsibility for regulatory quality or competition be given incentives to prepare an appropriate assessment?
- What resources are required for competition assessment?

It will become clear from what follows that there is no single or simple recipe for institutional implementation of competition assessment. Feasible solutions are likely to vary substantially across jurisdictions, given differences among

* This chapter was written by Sean F. Ennis and Rex Deighton-Smith.

jurisdictions with regard to such things as the extent to which there is a federal system, staffing strengths, and the political environment. While this Toolkit draws on existing experience to identify potential options, those options should not be considered exhaustive. As can be seen in the 2014 Report on the Implementation of the 2009 Recommendation¹ (Recommendation on Competition Assessment²), the implementation of the Toolkit was considered to be highly useful in a number of very different review exercises – impact assessment integrated into Regulatory Impact Assessment, discretionary assessments that might also be placed under the heading of competition advocacy and market and sector inquiries as well.

2. Which policies merit a competition assessment?

The depth of a competition assessment should be proportional to the extent of the potential negative competitive effects of a policy. The Competition Checklist permits a quick screening of policies so that those with the potential to unduly impact competition can be quickly identified for further assessment. Most individual laws or regulations do not have that potential. Consequently, most do not require a detailed competition assessment.

Laws, regulations and rules. Policies that may be subject to competition assessment include laws, regulations and rules that implement laws or regulations. Some governments and independent public bodies (such as national competition authorities, courts of auditors, etc.) have chosen to review competitive impacts of subsidies or of preferential treatment given to state-owned enterprises. Not all jurisdictions subject their laws to competition assessment, but those that have had the greatest success with competition assessment are the ones that have done so. (See Box 1.)

New and existing policies. Some governments have approached competition assessment by looking at both new and existing policies. This is the most effective way to broadly improve the competitive atmosphere, but requires substantial political will. Other governments have implemented a form of competition assessment focused exclusively on new policies.

¹ Experiences with Competition Assessment, OECD 2014, <http://www.oecd.org/daf/competition/Comp-Assessment-ImplementationReport2014.pdf>.

² OECD Recommendation on Competition Assessment, OECD 2009, <http://www.oecd.org/daf/competition/oecdrecommendationoncompetitionassessment.htm>

National, regional, local. There is a strong economic case for performing competition assessment at the national, regional, and local levels. Competition assessment is relevant to all government policies that may unduly restrict competition. Policies that create such limits are sometimes imposed at the national level, but they can also originate at the regional or local level. For example, policies hostile to competition in the provision of taxi services are often imposed at the local level while consumer-harmful regulation of professionals often occurs at the regional level.

Box 2. Australian National Competition Policy Reforms

After the completion of the Hilmer Committee's report in 1993 which urged greater microeconomic openness with a focus on pro-competitive reforms, Australian governments agreed in 1995 to a programme of reviewing and revising legislation that limited competition and that was not in the public interest. This reform programme resulted in the identification of 1700 laws that needed review. Legislation was reviewed at a national and state or territorial level, with most reviews being completed by 2001. The national government offered funding to aid state and territorial governments with any adjustment costs that might arise from revisions of legislation. The programme was notable because it systematically identified existing laws and regulations that merited review and because, during the implementation of the programme, Australia's GDP growth improved, relative to other OECD countries.

3. When should a competition assessment be performed in the policy development process?

New policies. Competition assessments can positively contribute to the design of new policies and ideally should be performed *early* in the policy development process, before a determination has been made about how to approach a given policy challenge. When a proposed policy has the potential to restrict competition, it is valuable to consult government competition experts early in the policy development process to ascertain whether alternatives can be developed that will achieve the regulatory objectives with less harm to competition.

Existing policies. Most existing policies have not been subject to a competition assessment. The critical issue here is prioritising which policies should be reviewed first, as it is almost inevitable that some existing policies are more likely to unnecessarily adversely impact competition than others. For example, in Australia at the time of its National Competition Reviews, hundreds of existing government policies were identified that limited competition. Australia prioritised these policies for review. Where problems were found, revision occurred in almost all cases.

4. Who should be involved with drafting and reviewing a competition assessment?

In order to ensure that competitive effects are properly considered, the governmental body developing the policy in question should perform the competition assessment. In that way, the right policymakers ask at the appropriate time the pertinent questions that are necessary to promptly and efficiently develop policies that take due account of competitive effects.

“Frontline” policymakers, however, may not take the competition assessment process seriously unless an external party reviews their work. Regulatory gatekeepers, officials with competition expertise such as those located in competition authorities, or some combination of the two can perform those reviews.

In the United Kingdom, the regulatory gatekeeper, the Better Regulation Executive (BRE), has responsibility for reviewing the impact of new regulatory proposals. Under guidelines published by the Department of Business in March 2015, regulations estimated to have a positive effect on competition can be counted as having net zero cost and are thus fast tracked through the impact assessment process. Policy makers also have discretion to assess whether or not their proposal will have a negative impact on competition. Departments can seek the advice of the Competition and Markets Authority (CMA), a competition authority, should their proposals raise competition concerns that require further analysis. The CMA also has the power to make Recommendations to ministers if it is concerned about the potential impact on competition of proposals for legislation.

To complete a competition assessment that is more comprehensive than required by the Competition Checklist would typically involve competencies related to market definition and competition analysis. For this reason, some countries require their competition authorities to review any new laws or regulations that are expected to have an economic impact before the provisions in question are enacted.

In Mexico, for example, the competition authority must review any new secondary legislation with potential effects on competition. In Korea, the competition authority has responsibility for reviewing selected new regulations. In Hungary, the competition authority is required to submit its comments on new regulations.

Many other countries hold horizontal consultations prior to the adoption of new regulations. Such consultations work better when competition reviewers can enter the process early and are not required to submit their comments on all policies, but

can intervene in situations in which they believe there may be a significant potential problem.

The reviewing body's degree of independence is also important. In Australia, for example, a new body was created in 1995 to oversee the National Competition Policy reviews of national and state or territory laws and regulations. This body, the National Competition Council, was created as a distinct and independent body from both the regulatory oversight office for reviewing new regulations and from the competition authority. Australia's success amply demonstrates the value of independent bodies reviewing laws and regulations.

Some national competition authorities, such as the former Spanish Comisión Nacional de la Competencia, have carried out reviews of subsidy schemes and published annual reports on subsidies.

A competition authority's or other government body's involvement in the competition assessment process should not bar any subsequent government legal action under that jurisdiction's competition laws. Competition assessments by definition are based upon predictions, and predictions in real life often turn out to understate competitive harms or overstate competitive benefits.

5. How can policymakers without responsibility for regulatory quality or competition be given incentives to prepare an appropriate assessment?

The policymakers who develop a new regulation may have an incentive to under-report potential competition problems associated with a proposed regulation. They may perceive that identifying a potential competition problem or consulting with an outside agency, such as a regulatory gatekeeper or a competition authority, simply creates more work for them without a substantial benefit. It is therefore important to emphasise to policymakers that competition assessment improves their product, the policy they make.

A number of options exist for enhancing policymaker's incentives to embrace and properly execute competition assessments, and their skills to perform that task. These options include:

- Including competition assessment in Regulatory Impact Analysis (RIA);
- Financial rewards; and
- Best-practice training.

5.1 *Including competition assessment in RIA*

RIA is a formalised process for reviewing regulations to ensure that they achieve their intended policy objectives. In general, the goal of RIA is for the benefits of a regulation to exceed its costs. RIA is more effective when competition assessment is included as one of its elements. That is because the dynamic, market-oriented considerations inherent in competition assessment provide important insights for a policymaker seeking to determine if the benefits of a particular regulation outweigh its costs. By 2009 over 30 members had RIA processes in place, and the competition element of the assessment was formally called Competition Assessment. Including competition assessment within RIA is an ongoing trend. In the United Kingdom, assessment of competition impact was introduced into RIA in 2002. In the European Commission, competition assessment has been part of the RIA process since 2005. In the United States, RIA guidance documents explicitly require consideration of market impacts.³ In 2013, Mexico included competition assessment as part of its RIA review process by its review body COFEMER. Giving the competition authority some role in this area also reduces the need for regulatory agencies or gatekeepers to retrain their staffs.⁴

It is the focus on dynamic market efficiency⁵ that makes competition assessment most useful as an element of overall regulatory assessment. This element can help avoid regulations that unduly restrict market activity. An additional, incidental benefit of competition assessment is that it helps identify all parties likely to be affected by a regulatory proposal, especially those who will be affected indirectly. This can assist officials in ensuring that RIA-based consultation is sufficiently inclusive and, thus, more effective.

The first step in conducting a full competition assessment within a RIA is to identify from the broader RIA process the underlying objective of the new regulation. Second, existing restrictions on competition should be identified and analysed. Then, an analysis should be made of what, and how substantial, are the proposal's adverse competitive effects. In some instances it may be helpful to

³ See Office of Management and Budget, Circular A-4, September 17, 2003.

⁴ For more details on how to include competition assessment in RIA, see DAF/COMP/(2007)8/REV1 "Integrating competition assessment into regulatory impact analysis"

⁵ Dynamic efficiency focuses on efficiency over time, with changes in efficiency resulting potentially from innovation, technological developments, the ability of firms to respond flexibly to new market conditions and growth of successful suppliers.

consider the current extent of competitive pressure, such as by defining a relevant market although this need not be a formal or elaborate process. Market definition is a tool to be used when it can be helpful, not a requirement. The main point is to be sure that the evaluator considers realistically what competition exists, and what competition is possible. Finally, the competitive effects of alternative policy options will be assessed and compared.

Most proposals will not harm competition significantly. Where, however, a competition assessment identifies significant potential for a weakening of competition in the affected industry or related industries, the key elements of the proposal's design should be reconsidered in a comparative context in which alternative means of achieving the regulatory objective that are less restrictive of competition are identified and assessed.

Where such alternatives cannot be identified, a rigorous, disciplined comparison of the proposal's benefits must be made. The proposal should be adopted only if that comparison shows that, after taking into account the costs of the anti-competitive impact the assessment identified, the proposal's enactment will yield a net benefit⁶.

5.2 *Financial rewards*

Because Australia is a federal system, implementing the National Competition Policy (NCP) at the state or territory level required the states' agreement. The Australian government made significant payments to states and territories, consisting of per capita payments based on the extent to which reviews and revisions of legislation were completed. "The NCP payments are the means by which gains from reform are distributed throughout the community. The payments recognise that, although the states and territories are responsible for significant elements of NCP, much of the direct financial return accrues to the Australian Government via increases in taxation revenue that flows from greater economic activity."

The payments to states and territories have been significant. Table 1 lists NCP payments since the introduction of the NCP.

⁶ This approach is already explicitly in use in Australia. The "Guiding Legislative Principle", adopted under the former National Competition Policy agreements states that legislation that restricts competition should not be adopted unless it can be shown both that the benefits of the restriction to the community as a whole outweigh the costs **and** that the objectives of the regulation cannot be achieved by any other means that is less restrictive of competition. See Competition Principles Agreement, clause 5 (1).

Table 1. Annual NCP payments received by jurisdictions (AUD million)

Jurisdiction	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06
	(a)	(a)	(a)	(a)	(a)	(a)	(a) (b)	(a) (b)	(b) (c)
New South Wales	126.5	138.7	148.6	155.9	242.5	251.8	203.5	233.6	292.5
Victoria	92.8	102	109.2	114.7	179.6	182.4	178.7	201.6	197.9
Queensland	74.2	81.6	81.5	73	147.9	138.9	87.9	143.3	178.7
Western Australia	38.4	42.4	43.2	45.5	71.1	72	33.6	53.5	71
South Australia	34.3	38.4	34.5	35.9	55.7	57.1	40.7	50.4	54.3
Tasmania	12.6	13.9	10.8	11.2	17.4	17.7	17.2	19.8	19
ACT	6.2	7	7.2	7.5	11.6	12.4	11	13.6	12.7
Northern Territory	11.2	13	4.5	4.5	7.6	7.5	5.9	8.4	8
Total	396.2	436.9	439.5	448	733.3	739.9	578.5	724.2	834.1

Source: National Competition Council

- (a) From Final Budget Outcome documents.
 (b) Each jurisdiction's payments reflect the application of permanent deductions and suspensions.
 (c) Costello, the Hon. P (Treasurer) 2005, 'National Competition Payments to States and Territories for 2005', Media release, 15 December 2005.

Note 1: Totals may not add due to rounding

Note 2: Figures up to and including 1999-2000 include Financial Assistance Grants

While the payments are significant, the Australian government has estimated the annual benefits to the economy to be 2.5% of GDP, or 20 billion AUD, from productivity improvements and price rebalancing in many different sectors where NCP and related reforms have occurred.⁷

⁷ See Productivity Commission (2005) *Review of National Competition Policy Reforms*, Productivity Commission Enquiry Report No. 33, 28 February. The review notes that direct causal links are difficult to establish empirically. Moreover, measuring net impacts in this area is particularly complex.

5.3 *Best practice*

The provision of training on best practices for policymaking officials doing, or reviewing, the work is critical for the success of a competition assessment programme. Many policymakers are specialised in a domain that does not relate to competitive effects or economics. Such officials cannot be expected to assess competition issues appropriately without specific training. Competition authorities, regulatory gatekeepers, or the OECD can help with that effort.

6. **What resources are required for competition assessment?**

The resources necessary for an effective competition assessment programme can be relatively small. For example, when the United Kingdom implemented its competition assessment programme, two staff members from the OFT played a very active role, and only a small percentage of the roughly 400 regulations reviewed per year received detailed scrutiny. The rest were assessed by means of a competition filter, akin to the Competition Checklist reviewed in Chapter 1, which permitted officials to quickly diagnose whether there was a significant chance that competition problems would materialise from the policy.

Of course, a competition assessment programme can also benefit from a high level of resource commitment. The Australian example illustrates a far-reaching and resource intensive approach that has coincided with a strong economic performance.

Regardless of level of commitment, resource requirements will be highest at the initial implementation stage. A detailed programme of best practice training, for example, most often requires a large initial one-time expenditure of resources. Training in later years, however, would not have to be as substantial, as the system will be better functioning and personal relationships between relevant policy officials already will have been established. However, due to staff turnover, ongoing training almost certainly will still be needed after the initial implementation.

7. **Conclusion**

The incorporation of competition assessment into government regulatory decision making has the potential to yield strong economic benefits by identifying areas where market activity is unduly restricted and suggesting policy alternatives that will continue to meet policy goals while promoting competition to the extent possible. Given that the institutional, legal and federal environments of OECD jurisdictions differ substantially, how competition assessment best fits within government operations will likely vary from one jurisdiction to another. But a few points stand out. First, regulatory gatekeepers are well-suited to perform competition

assessments, particularly when they are being done as a part of a RIA. Second, competition authorities are ideally suited for advising on competition assessments, providing training regarding the process, and performing selective competition assessments. Finally, the benefits from fitting an effective competition assessment programme into government regulatory operations are definitely worth the costs.

APPENDIX

On October 22, 2009, the Council of the OECD adopted a recommendation on competition assessment. The text of the recommendation follows.

RECOMMENDATION OF THE COUNCIL ON COMPETITION ASSESSMENT

THE COUNCIL,

Having regard to Article 5 b) of the Convention on the Organisation for Economic Co-operation and Development of 14th December 1960;

Having regard to the agreement reached at the 1997 Meeting of the Council at Ministerial level that restrictions on competition are often costly and ineffective in promoting public interests and should be avoided [C/MIN(97)10];

Having regard to the OECD Guiding Principles on Regulatory Quality and Performance [C(2005)52], which call for governments to review proposals for new regulations, as well as existing regulations, with reference to competition;

Recognising that competition promotes efficiency, helping to ensure that goods and services offered to consumers more closely match consumer preferences, producing benefits such as lower prices, improved quality, increased innovation and higher productivity;

Recognising that higher productivity is essential to economic growth and increased employment;

Recognising that public policies serve a variety of commercial, social, health, safety, security environmental and other objectives;

Recognising that, at times, public policies unduly restrict competition;

Recognising that such undue restrictions can occur unintentionally even when the public policies in question are not focused on economic regulation and not intended to affect competition in any way;

Recognising that public policies that unduly restrict competition often may be reformed in a way that promotes market competition while achieving the public policy objectives;

Recognising that regulation and reform of regulated industries usually require detailed competition assessment of likely effects;

Recognising that, other things being equal, public policies with lesser harm to competition should be preferred over those with greater harm to competition, provided they achieve the identified public policy objectives;

Noting that a number of countries already perform competition assessment; and

Noting that the OECD and a number of OECD Member countries have developed competition assessment toolkits;

I. RECOMMENDS as follows to governments of Member countries:

A. Identification of existing or proposed public policies that unduly restrict competition

1. Governments should introduce an appropriate process to identify existing or proposed public policies that unduly restrict competition and develop specific and transparent criteria for performing competition assessment, including the preparation of screening devices.
2. In performing competition assessment, governments should give particular attention to policies that limit:
 - i) The number or range of market participants;
 - ii) The actions that market participants can take;
 - iii) The incentives of market participants to behave in a competitive manner;
 - iv) The choices and information available to consumers.

3. Public policies should be subject to competition assessment even when they pursue the objective of promoting competitive outcomes and especially when they:
 - i) Set up or revise a regulatory body or regime (e.g., the assessment could make sure that, among other things, the regulator is appropriately separated from the regulated industry);
 - ii) Introduce a price or entry regulation scheme (e.g., the assessment could make sure that there are no reasonable, less anticompetitive ways to intervene);
 - iii) Restructure incumbent monopolies (e.g., the assessment could make sure that the restructuring measures actually achieve their pro-competitive objectives);
 - iv) Introduce competition-for-the-market processes (e.g., the assessment could make sure that the bidding process provides incentives to operate efficiently to the benefit of consumers).

B. Revision of public policies that unduly restrict competition

1. Governments should introduce an appropriate process for revision of existing or proposed public policies that unduly restrict competition and develop specific and transparent criteria for evaluating suitable alternatives.
2. Governments should adopt the more pro-competitive alternative consistent with the public interest objectives pursued and taking into account the benefits and costs of implementation.

C. Institutional Setting

1. Competition assessment should be incorporated in the review of public policies in the most efficient and effective manner consistent with institutional and resource constraints.
2. Competition bodies or officials with expertise in competition should be associated with the process of competition assessment.
3. Competition assessment of proposed public policies should be integrated in the policy making process at an early stage.

D. Definitions

For the purposes of this Recommendation:

“public policies” means regulations, rules or legislation.

“unduly restricts competition” means that restrictions on competition needed for achieving public interest objectives are greater than is necessary, when taking into account feasible alternatives and their cost.

“market participants” means businesses, individuals or government enterprises engaged in supplying or purchasing goods or services.

“competition bodies” means public institutions, including a national competition authority, charged with advocating, promoting and enhancing market competition and not limited in these roles to a specific sector.

“competition-for-the-market processes” refers to the bidding processes organised by government for allocating the right to supply a given market or for using a scarce government resource for a distinct period of time.

“competition assessment” means a review of the competitive effects of public policies including consideration of alternative and less anti-competitive policies. The principles of competition assessment are relevant to all levels of government.

II. INVITES non-Member economies to associate themselves with this Recommendation and to implement it.

III. INSTRUCTS the Competition Committee:

To serve as a forum for sharing experience under this Recommendation for Member countries and non-Member economies that have associated themselves with this Recommendation;

To promote this Recommendation with other relevant Committees and Bodies of the OECD;

To report to Council in three years on experience with this Recommendation.

The Competition Assessment Toolkit Vol. 1 Principles and Vol. 2 Guidance are available for download in the following languages:

www.oecd.org/competition/toolkit

Arabic / العربية	Italian / Italiano
Chinese / 中文	Japanese / にほんご
Croatian Hrvatski	Korean / 한국어
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For further information about the Competition Assessment Toolkit, please contact us at DAFCOMPContact@oecd.org or visit www.oecd.org/competition/toolkit