OECD Reviews of Regulatory Reform

POLAND

FROM TRANSITION TO NEW REGULATORY CHALLENGES



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2002

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Foreword

The OECD Review of Regulatory Reform in Poland *is one of a series of country reports carried out under the OECD's Regulatory Reform Programme, in response to the 1997 mandate by OECD Ministers.*

Since then, the OECD has assessed regulatory policies in 16 member countries. The reviews aim at assisting governments to improve regulatory quality – that is, to reform regulations to foster competition, innovation, economic growth and important social objectives. It draws on two important instruments: the 1995 Recommendation of the Council of the OECD on Improving the Quality of Government Regulation *and the 1997* OECD Report on Regulatory Reform.

The country reviews follow a multi-disciplinary approach and focus on the government's capacity to manage regulatory reform, on competition policy and enforcement, on market openness, and on the regulatory framework of specific sectors against the backdrop of the medium-term macro-economic situation.

Taken as a whole, the reviews demonstrate that a well-structured and implemented programme of regulatory reform can make a significant contribution to better economic performance and enhanced social welfare. Economic growth, job creation, innovation, investment and new industries are boosted by effective regulatory reform, which also helps to bring lower prices and more choices for consumers. Comprehensive regulatory reforms produce results more quickly than piece-meal approaches; and they help countries to adjust more quickly and easily to changing circumstances and external shocks. At the same time, a balanced reform programme must take into account the social concerns. Adjustments in some sectors have been painful, but experience shows that the costs can be reduced if reform is accompanied by support measures, including active labour market policies.

While reducing and reforming regulations are key elements of a broad programme of regulatory reform, experience also shows that in a more competitive and efficient market, new regulations and institutions may be necessary to ensure compatibility of public and private objectives, especially in the areas of health, environment and consumer protection. Sustained and consistent political leadership is another essential element of successful reform, and a transparent and informed public dialogue on the benefits and costs of reform is necessary for building and maintaining broad public support.

The policy options presented in the reviews may pose challenges for each country. However, the in-depth nature of the reviews and the efforts made to consult with a wide range of stakeholders reflect the emphasis placed by the OECD on ensuring that the policy options presented are relevant and attainable within the specific context and policy priorities of the country.

Each review consists of two parts. Part One presents an overall assessment, set within the macro-economic context, of regulatory achievements and challenges across a broad range of policy areas: the quality of the public sector, competition policy, market openness and key sectors such as telecommunications and energy. Part Two summarises the detailed and comprehensive background

reviews prepared for each of these policy areas, and concludes with policy options for consideration which seek to identify areas for further work and policy development in the countries under review. The background reviews are available on the OECD Web site: www.oecd.org/regreform/backgroundreports

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Executive Summary

Poland's transition to a democratic market economy is, in broad terms, mostly complete.

The country has changed beyond recognition compared to what it was in 1989 after the fall of communism. Accession to the EU has been, and remains, a key driver of modernisation and reform. However important challenges remain. It is important that Poland's own commitment to reform should continue and that it should not succumb to reform fatigue.

The democratisation of state institutions has been fully achieved.

The initiation and implementation of public policy is democratically based. The executive, judicial and legislative powers are constitutionally separated. There is a free and lively press. The creation of an almost entirely new framework of democratically accountable state institutions culminated in the adoption of a new Constitution in 1997. The adoption of a Freedom of Information Act in September 2001 should boost government accountability and transparency, if the Act is well implemented. Devolution of powers to local government was an important and supportive part of the democratisation of the state, but does raise problems of ensuring effective public service and regulation at the local level, and there is some evidence of corruption, which must be tackled.

The market economy is developing well, but remains a "work in progress".

Important successes include the emergence of a robust financial system (one of the best in the region), trade liberalisation, which culminated in Poland's accession to the WTO as a founding member, and price deregulation. Private entrepreneurship has developed strongly. But other important reforms have been delayed, such as privatisation, the restructuring of many large state-owned companies and effective regulatory reform of the network industries.

An effective competition policy has helped to shape the new market economy.

Poland took early steps (in 1990) to establish an effective competition law and competition authority. The latter has been a committed advocate in support of the structural and liberalisation reforms so far. The law has recently been further strengthened and brought fully into line with EU law. An important challenge now is to help curb inefficient interference in the market economy through state aids and subsidies.

Fundamental economic reforms have strengthened the economy and brought unprecedented economic prosperity.

GDP growth averaged 5.5% pa between 1994 and 2000, one of the highest in the OECD. This performance underlines the effectiveness of the government's reform programme in improving resource allocation and so raising productivity. Monetary policy has been tackled, and a clear, sound framework is in place to control inflation. The goal to reduce headline consumer price inflation to below 4% by the end of 2003, consistent with the government's wish to adopt the Euro in due course, was achieved by the end of 2001. Radical reforms in the management of public finance have been engaged, based on sound principles. These include the introduction of the Constitutional debt ceiling in 1997, reinforced by the 1998 Public Finance Act, and the government's "Strategy of Public Finance and Economic Development 2000-2010" which also focuses on five key reform areas: pensions, health care, education, taxes, and decentralisation.

The central administration of government has been substantially overhauled.

A comprehensive administrative framework and principles are now in place. The objectives have been to adjust the centre to local government devolution, reduce a large and inefficient bureaucracy, remove overlap of responsibility between ministries, and create horizontal structures to facilitate co-operation and the resolution of differences. The government has also embarked on more specific reforms to improve regulatory quality and created mechanisms to promote harmonisation of laws with those of the EU.

The combination of economic and regulatory reforms has already brought significant achievements.

These include an enormous expansion of private sector activity, and a boom in foreign direct investment. Today the private sector generates 70% of GDP and employs 72% of workers. Foreign investment interest in Poland gathered pace after 1995, encouraged by the reforms. Its stock approached USD 50 billion in 2000. Restructuring and reform of the financial system has been a great success. The transformation was greatest in the banking sector based on strong new primary legislation which restructured the sector and created an effective supervisory framework. The creation of a modern stock market has been another major achievement. A modern insurance market has also been established. A new market in pension funds took off with changes in pension policy.

But Poland's great economic leap forward now needs to be consolidated.

Economic performance remains vulnerable. Key issues are the internal and external deficits, and unemployment. The current account deficit is a weak spot in economic management and the internal fiscal deficit is a recurring issue. There are problems of

implementation in the reforms of the pension, health and education systems. Reform of taxation so far only covers corporate taxation. More reforms are needed to boost job creation. Human resources continue to be underused, and unemployment remains a major challenge (reaching over 16% in 2001) Improving productivity has led to a significant shedding of excess labour, but not enough new jobs have been created because of labour market rigidities including high labour taxes among other problems. Further structural and regulatory reform is needed to address specific weaknesses such as the slow progress in dismantling and restructuring the state-owned monopoly sectors, and unnecessarily burdensome regulations on business.

There is also a need to consolidate the regulatory reforms already undertaken.

Major challenges still lie ahead in further improving the state's regulatory capacities. The pace of change has been enormous, and there is now a pressing need to address the quality of human resources harnessed to reform, building on the efforts which have already started to create a more professional civil service. The quality of regulation also needs attention, using better administrative tools and more consultation. The government's introduction of an RIA system in late 2001 is an essential addition to the current regulatory framework and very encouraging. But the new framework and procedures need to be tested. The decentralisation process and local government institutions need special attention. Initiatives are needed to raise competence and skills at the local level, and better supervision of local administration needs to be put in place. Co-operation between the different levels of government is poor, and the quality of local regulation an urgent issue. A review of attitudes to transposing EU laws may be desirable. EU directives may represent the lowest common standard to be achieved, not necessarily best international practice.

Implementation, enforcement and compliance must not be neglected.

This is especially important. An impressive amount of new legislation has built up which must be well implemented if it is to have an effect. Efforts to tighten up on regulatory abuse – excessive and poorly applied administrative discretion, and corruption – are needed. Delays in court proceedings also need to be tackled more vigorously. Steps to reduce inefficiency and under-financing of the judiciary have already been taken but will need to be reinforced. Implementation also means putting necessary secondary legislation in place as soon as possible to flesh out and give full effect to the new laws.

Vigorous private sector activity is a cornerstone of the economy: to keep this up the environment for SMEs needs further improvement.

The 1999 Business Law was a major reform. But obstacles to entrepreneurship remain. Remaining regulatory obstacles include restrictive staff regulations, excessive discretion in the allocation of funds, which is distorting effective competition, complicated tax regulations and "red tape".

Some sectors of the economy need an adjustment, development or radical overhaul of regulation.

The regulation of the pension fund market needs attention. Corporate governance would be helped by a new bankruptcy law. Regulatory reform is needed to promote an expansion of the intercity road network. The remaining state monopoly sectors need a more courageous approach to liberalisation**.** Liberalisation of the state sector is perhaps the most incomplete element of the reform agenda to date. Many state- owned companies continue to benefit from significant advantages compared with the private sector. Many large state-owned sectors (such as post and gas) received little attention in the reforms of the early 1990s. This now needs attention. Restructuring, privatisation, regulatory reform and liberalisation have so far been tackled with varying enthusiasm. They need to be accelerated.

The need for further change appears to have been recognised by the government.

Since fall 2001, the government has started initiatives to put the country back on the path of economic growth**.** The public deficit is being addressed, and will be allowed to rise by no more than 1% in real terms (though this ceiling does not cover the whole public sector budget). Government restructuring has also taken place, reducing the number of institutions. A series of measures to spur entrepreneurship and employment is also proposed, together with stronger restructuring plans for the energy, rail transport and defence industries, among others. This is encouraging, if the plans are followed through.

Regulatory reform is essential for Poland to continue on the path of sustained economic growth.

It has already proved its worth. Important and positive links exist between regulatory reform, entrepreneurship, structural change and employment. These must continue to be nurtured.

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PART I

Regulatory Reform in Poland

PART I

Chapter 1

Performance and Appraisal

Abstract. *Like other central and eastern European countries, Poland underwent fundamental change in the 1990s as it made the transition from a planned to a market economy. The liberalisation of economic activity and the democratisation of government institutions were deep and strong. Today Poland has a functioning market economy together with a democratic framework of state institutions, with the EU accession process fostering further liberalisation and modernisation. However, this is only the "end of the beginning". Achievements, especially in economic performance, need to be consolidated, and new legislation must be implemented in an efficient manner. Major challenges lie ahead in enhancing the state's regulatory capacities; these include improving the quality of human resources in the public sector and the effectiveness of regulation at all levels of government. Liberalisation of the remaining state monopolies calls for a more courageous approach and points to the need for further regulatory reform in support of the structural changes required in these sectors. A business environment more conducive to entrepreneurship is also desirable. The key message of this review is the necessity for continuous reform.*

Introduction

Poland's transition to a democratic market economy is, in broad terms, mostly complete

Poland's transformation from a planned to a market economy started in earnest in 1990. Earlier changes under the communist regime were partial and without much improvement to the regulatory environment. By the end of the 1980s Poland had come to be characterised as having "neither plan nor market", and was in a state of deep crisis, with severe balance of payments and debt repayment problems, and a hyperinflationary spiral of prices and wages. There was no alternative but to reform.

The reforms of the 1990s to stabilise the economy, liberalise economic activity, and transform state institutions were far-reaching – as they had to be – and successful in creating the foundations of a new state and economy. Though output fell at first, the fall was less marked and the subsequent growth higher and more sustained than in other countries making the transition from communism. Output growth was based on productivity gains attesting to successful economic reforms that had led to better resource allocation, a dynamic private sector, and a massive flow of foreign direct investment (FDI) which brought with it advanced technology and management know-how.

In its broad strategic lines Poland's transition to a democratically based market economy is mostly complete. After the first round of massive change at the start of the 1990s the reforms came in waves. The transition proceeded on five fronts:
1) transferring state powers to democratic institutions 2) implementing an economic reform programme to create a free market 3) devolving powers to local government 4) setting the objective of joining the European Union (EU) and 5) reforming the administrative and regulatory capacities of the state. However important challenges remain and parts of this programme are today much more successful and complete than others.

Since fall 2001, the government has undertaken a number of initiatives to put the country back on the path of economic growth

Some of the issues that still need attention have been the subject of a new focus over the last few months. The government has put in place an important programme to promote the conditions for renewed economic growth. The first part addresses the public deficit. The government deficit is estimated to have more than doubled in 2001 reaching 5% of GDP. To counter this, public spending will be allowed to rise by no more than 1% in real terms. But this only applies to State budget expenditure which accounts for just 40% of spending, so it is difficult to judge the potential impact on overall spending. Steps have also been taken to restructure the government including reductions in the number of ministries, a public-sector wage freeze, the elimination of more than 20 central offices and agencies, some employment cuts and other savings measures.

The second part of the government's programme involves efforts to stimulate economic development and improve labour market performance. Dubbed a "1-3-5" plan (after the rates of growth the programme anticipates during the period 2001-2004), the programme emphasises a series of measures to spur entrepreneurship and employment. Proposed regulations will be subjected to a cost benefit analysis, the rights and obligations of both taxpayers and fiscal authorities will be clarified, the tax system will be simplified regionally and age differentiated minimum wages will be introduced and business registration procedures will be simplified. The "First Job" component of the programme centres on a series of job creation measures aimed at facilitating the hiring of school leavers and graduates.

The scheme also covers restructuring plans for particular industrial sectors including the mining, electricity, oil and gas, rail transport and defence industries. To this end, the Economy Ministry has drafted proposals for the radical restructuring of the gas and electricity companies, to break up current monopolies in both sectors. The government has also announced that it will accelerate the privatisation of power plants, with the exception of a few crucial ones that would remain under the control of the Treasury. The government has also stepped up the pace of EU accession negotiations in an effort to ensure Poland's participation in the first group of candidate countries.

These proposals represent an encouraging further development of regulatory reform. Well implemented they should pave the way towards a more rapid economic recovery and an improved business environment.

Democratisation of state institutions has been fully achieved, but corruption is an issue

The democratisation of the state is effectively complete. The government and its administration no longer exert centralised and authoritarian control over economic and social life: the initiation and implementation of public policy is democratically based. The executive, judicial and legislative powers are constitutionally separated. There is a free and lively press. The new Freedom of Information Act, if it is effectively implemented, should give an important boost to the government's accountability. The only shadow on this heroic achievement is the evidence of some corruption.

The free market economy is developing well, but remains a "work in progress"

The establishment of a free market economy is well advanced, and remaining challenges are similar to those facing many OECD countries. Poland started the process as the weakest of the economies of Central and Eastern Europe, with inflation at 40% a month, and a foreign debt of over USD 40 billion. The government's "shock therapy" which cut state subsidies, lifted nearly all price controls and deregulated the economy put massive strains on the economy and society. But after painful adjustments the economy recovered from 1994 onwards, and the country enjoyed rapid and sustained growth and reduced inflation. Economic imbalances nonetheless remain, such as high unemployment (15% and higher than neighbouring countries at the end of 2000) and a failure to contain the current account deficit.

Important successes for the market economy have been achieved, notably the emergence of a robust financial system (one of the best in the region) thanks to new laws and institutions, trade liberalisation which culminated in WTO accession (Poland is a

founding member) and price deregulation. These measures gave a huge boost to private entrepreneurship, which already had strong roots in Polish history. But other equally important reforms have been delayed, such as privatisation, which only started on a large scale in 1997, the restructuring of many large state-owned companies and regulatory reform of the network industries.

Devolution of powers to local government raises important problems which must be tackled

The devolution of powers to local government (regions, counties and municipalities) was an important and supportive part of the democratisation of the state, and marked a watershed with the communist era when all decisions were taken centrally. It has been significant in scope, with the establishment of local budgets, a key constitutional provision that "local self-government shall perform public tasks not reserved by the constitution… to other public authorities", and the ability to access EU funds directly. It has transformed the relationship between different levels of government.

One notable achievement is the improvement of local public infrastructure using EU funds. But the change has enormous implications for public service provision and regulatory functions, which have not yet been fully mastered or digested. Co-operation between the different levels is poor, and the quality of local regulation an urgent issue.

Accession to the EU remains a key driver of modernisation and reform

The ambitious objective, set in 1991 with the signature of an Association Agreement, to put Poland on a fast-track course to join the EU is being pursued with substantial success. About 3 900 directives, regulations and other instruments must still be transposed into Polish law.

The need to adapt laws and regulations to fit the EU's "acquis communautaire" has been a strong and positive force in transforming the regulatory and administrative landscape for the better. The link with the EU, and membership of other international organisations such as WTO (1995), OECD (1996) and NATO (1999) has opened up the economy and society. Membership of these international organisations can help with insights into international best practice and help overcome domestic resistance to change.

The EU has an especially strong influence. The need to adapt is driving much needed structural and liberalisation measures, especially in the still largely monopolistic network industries of electricity, gas, postal services and telecommunications. A big training programme for legal and administrative staff has been implemented. But progress is a little slow, though accelerating. And the immensity of the work means that the quality of new legislation has sometimes suffered.

Major challenges need to be tackled in reforming the state's regulatory capacities, including effective implementation

Finally, but not least, the fifth strategic pillar of reforming the administrative and regulatory capacities of the state is engaged, but is slow and incomplete. It has taken longer than other reforms, partly because it is so complex. However three crucial foundation stones are now in place.

First, the new constitutional framework, which culminated in the 1997 Constitution, not only confirmed the strong foundations of democracy. It also triggered a major review of existing laws and regulations and eliminated major inconsistencies. Second, the operation of government has been the subject of a major restructuring initiative launched in 1996 with the State Economic Administration Reform and the Law on the Organisation and Rules of Procedure of the Council of Ministers and on the Scope of Competence of Ministers (the Law on Organisation). Third, a better regulatory management system and new institutions to steer it, including the strengthening and creation of bodies such as the Government Legislative Centre, the Debureaucratisation Task Force (1997-2001) and the Regulatory Quality Team (since 2001), have been developed to improve regulatory quality.

But these reforms are very incomplete, not least because some of them are quite recent: it is hard to say at this stage how effective they will be in improving the regulatory landscape. Despite progress, a number of challenges are clearly visible. The body of primary legislation still lacks coherence, and is unstable, with repeated amendment of laws. The quality of laws is patchy, and too much discretion in their application is often built in. However public consultation during the law- and rule-making process should now be enhanced with the recently adopted Freedom of Information Act (which entered into force on 1 January 2002).

Just as important, there is a pressing need to expand efforts from the current focus on making legislation – without losing sight of this and of the need to improve its quality– and address the issues of effective implementation, enforcement and compliance. The body of new legislation that has accumulated over the last few years of reform is impressive, but loses much of its value if it is not well applied.

The macro-economic context for regulatory reform

The 1990s saw a period of unprecedented strong growth and economic prosperity flowing from successful early reforms

Poland's transformation started with the "shock therapy" introduced by the government that came into power at the end of 1989. This was in response to a crisis that threatened to engulf the country in economic chaos, requiring emergency stabilisation measures. The government acted quickly and strongly across a broad front: from immediate liberalisation of prices and trade to changing the legal basis for economic activity in such areas as property rights, banking and competition law. Deregulation was a major theme. Legal and institutional reforms followed.

Foreign Direct Investment (FDI) has played an important role in the growth process since the mid-1990s as awareness grew of Poland's sound fundamentals, nurtured by earlier reforms. Its stock approached USD 50 billion in 2000. Green-field manufacturing projects were particularly targeted, as well as banking and retail trade, largely for the domestic market (over 200 large foreign supermarkets can now be found in the suburbs of major cities).

After the inevitable – and painful – adjustment, the 1990s saw a period of unprecedented economic prosperity. Gross domestic product (GDP) growth averaged 5.5% pa between 1994 and 2000, one of the highest in the OECD and much higher than that of neighbouring economies. This performance is a testimony to the effectiveness of the government's reform programme in improving resource allocation, leading to productivity gains. Overmanning was sharply reduced, and the participation of skilled workers increased. Capital investment also played a role, with investment expanding rapidly to reach 26% of GDP, one of the highest in the OECD. The manufacturing sector was a major beneficiary, and its productive capacity became more efficient as equipment was replaced.

Monetary policy has been tackled, and a clear, sound framework is in place to control inflation

Monetary policy was the subject of a very effective reform in 1998: a clear long-term framework for monetary policy was adopted, and the independent Monetary Policy Council (MPC) of the Central Bank was given decision-making authority on interest rates and

Table 1. **GDP Growth, 1996-2000**

	Real GDP growth[1]	Growth of GDP deflator		
		Average[1]	1996	2000
Poland	5.1	11.6	18.7	7.1
Czech Republic	0.9	6.2	8.8	0.9
Hungary	4.0	13.8	21.2	9.1
Slovak Republic	4.1	5.8	4.5	6.5
EU	2.6	1.8	2.5	1.5
OECD	3.2	3.2	4.2	2.6

1. Average annual growth.
Source: OECD (2001), *Economic Outlook* No. 70, Paris.

setting inflation targets. It adopted the Medium-term Monetary Policy Strategy in 1998 which aims to reduce headline consumer price inflation to below 4% by the end of 2003, consistent with the government's wish to adopt the euro in due course. Indeed, even if inflation is expected to increase somewhat over the near term, it had already been brought below this level by the end of 2001, and appears under control.

The current account deficit is a weak spot in economic management

A rising current account deficit, which reached a peak of 8.1% of GDP in 1999, has been a matter of concern, even if a large part of the deficit has been financed by FDI inflows. Concerns about financial instability, however, have been mitigated by the subsequent economic slump which reduced it to 6.2% in 2001. But the fragility remains as repeated fiscal slippage could undermine foreign investors' confidence.

The internal fiscal deficit is a recurring issue

While Poland has generally succeeded in avoiding the high general government deficits (central and local government plus social security) that have plagued some of its neighbours, it is burdened with a high level of debt (which accrued mainly prior to transition from communism). While the overall deficit has hovered around 3% of GDP over much of the transition, it increased rapidly in 2001, reaching an estimated 4.5% of GDP. In addition, debt servicing charges are set to increase by as much as 1 or 2% of GDP from 2004 onwards, as the low interest London and Paris club loans mature and are rolled over. This means that unless steps are taken to bring government spending under control, Poland risks overshooting the debt ceiling introduced as part of the new Constitution of 1997 and the 1998 Public Finance Act. Indeed at the end of 2001 gross public debt represented debt over 40% of GDP.

Radical reforms in the management of public finance have been engaged, based on sound principles

The persistent government deficit led to the introduction of the Constitutional debt ceiling in 1997, reinforced by the 1998 Public Finance Act which clarified budgetary responsibilities, promoted greater transparency in public finances, established rules for local government, and prepared a road for accession to the EU. It was the basis for the government's adoption of "The Strategy of Public Finance and Economic Development. Poland 2000-2010" in June 1999. This called for an improvement in the quality of public services, shifting the balance of public expenditure from social transfers to investment,

Table 2. **Current account deficit/GDP, 1996-2000**

	Average	1996	2000
Poland	–5.0	–2.3	–6.3
Czech Republic	–4.7	–7.1	–4.5
Hungary	–3.6	–3.8	–2.9
Slovak Republic	–7.7	–10.6	–3.8
EU	0.6	0.9	–0.4
OECD	–0.4	0.0	–1.3

Source: OECD (2001), *Economic Outlook* No. 70, Paris.

and reducing the tax burden. The Strategy also focuses on structural and fiscal policy and other issues. The five key pillars of the Strategy are reform of pensions, health care, education, taxes, and decentralisation.

Reforms of the pension, health and education systems draw on experience elsewhere, but there are problems of implementation

Considerable progress has been made in reforming the inefficient mandatory old age pension system. Old age pensions were separated from other pensions, and a new system introduced in 1999. This is based on individual accounts, lowers the net present value of debt to both current and future pensioners, changes the nature of pension contributions from quasi-taxes to quasi-savings, and reduces incentives to retire early and under-report income. With the size of pension fund assets already around USD 3.5 billion, and projected to reach one third of GDP in 20 years, investments by the pension funds should contribute to the further development of financial markets. But there are serious institutional problems implementing the new system, and the rest of the social security system is not yet reformed.

A new social health insurance system was also introduced in 1999, marking a radical change from a centrally controlled, budget-based system to a decentralised, insurance-based system operated through regional health funds and competition between service providers. As with the pension reforms, the principles behind the changes are admirable, drawing on the experiences of other countries. But the new system has not met with the approval of public opinion, and some of the regional funds have encountered financial problems. Some of these problems may be transitory, but others demand further reform efforts, including improved governance of public hospitals and regional health funds.

The reform of the education and training system was also started in 1999 and aims at increasing participation in secondary and tertiary education, developing practical skills, increasing access to education for the rural population, adapting vocational training to business needs, and improving the financial situation of the educational system. A key way in which the government hopes to promote a more effective system is by decentralising tasks to local government. This will need to be handled with care to ensure quality results.

Reform of taxation so far only covers corporate tax, but more reforms are needed to boost job creation

The reform of taxation also started in 1999. It has focused on indirect and corporate income taxes, but left personal taxation relatively untouched. The reform of corporate tax was necessary given high effective rates compared to other countries in the region. The plan is to reduce rates to 22% by 2004 (from 34% in 1999), and the complex system of investment allowances has been abolished (previously acquired rights have been preserved). Despite these reforms, the system still favours non-incorporated companies whose profits are only taxed under the personal income tax system, unlike incorporated companies that face both a corporate income tax and personal income tax on distributed earnings. However, recent and further planned reductions in the corporate income tax rate should reduce the extent of the bias. An Enterprises Income Tax Act is planned, which would equalise the corporate burden on all enterprises. However, the failure to reform personal income tax, combined with high social security contributions, still leaves firms

facing high labour taxes, which discourages job creation by companies and encourages work in the informal sector.

Human resources continue to be underused, and unemployment is a major challenge

The effective use of human resources in the economy is a major challenge. Unemployment has been a key problem since the early 1990s. It reached over 16% during the course of 2001, with a large number of school leavers entering the labour market. While the growth slowdown contributed to that increase, the high and rising level of unemployment (even in years of rapid growth) suggests that structural factors underline the current joblessness. Thus, while improving productivity has led to a significant shedding of excess labour, not enough new jobs have been created because of labour market rigidities including high labour taxes, a regionally-non differentiated minimum wage, regulatory obstacles to the renewal of fixed-term contracts, and mismatches between skills offered and required. The effectiveness of current policies to reduce unemployment is low and a reassessment leading to further reforms is urgently needed.

A further problem of human resource under-utilisation is low labour participation, or inactivity. Policies to reduce the labour force by encouraging early retirement in the 1990s with generous pensions led to a large number of retired people, who remain inactive (though the recent pension reform changed this). Generous sickness pensions also encourage inactivity. Social protection is among the highest in the region. Even though this is one of the reasons why income inequality is among the lowest in the region, it discourages labour market participation.

However the official data probably overstate the amount of inactivity, as many people work in the informal economy. A large informal economy was a legacy of communist days and helped to develop business skills that were subsequently put to good use. But this transition is over and informal activity is now harming the economy by forcing the government to charge higher (and therefore more distorting) tax rates on those firms and individuals that operate within the informal economy so as to make up the revenue shortfall. The higher taxes create a vicious circle by increasing incentives to work in the underground economy. But by the same token, they hold out the possibility of creating a virtuous circle of reduced taxes and increased formal activity, which would be easier to set in motion if tax administration were improved and the bases upon which taxes were levied were widened.

Table 3. **Unemployment rate in Poland, 1996-2000**

	Average	1996	2000
Poland	12.8	12.3	16.1
Czech Republic	6.6	3.9	8.9
Hungary	8.1	10.1	6.5
Slovak Republic	14.2	11.3	18.8
EU	9.6	10.6	8.1
OECD	6.8	7.3	6.2

Source: OECD (2001), *Economic Outlook* No. 70, Paris.

The fifth major pillar of the Public Finance and Economic Development Strategy consists of seeking a new balance between the centre and the local levels of government. As part of the democratisation of the State, the first round of devolution of powers to level the municipalities and regions started in 1991 and restructuring the administrative divisions of the country was also carried out.

1991 also saw the start of an ambitious fast track course to join the European Union, a process involving the adaptation of Polish legislation to the structure and content of the EU legal framework, as well as a overhaul in terms of implementation, including the education of judicial staff and other state officials to ensure the capacity to do this.

In sum: the great economic leap forward of the 1990s needs to be consolidated by tackling the internal and external deficits and unemployment, requiring further structural and regulatory reform

Many of the key issues in building and sustaining a strong economy have been energetically tackled on the basis of sound principles, not least the policy to contain inflation (with the establishment of an independent institution to fix interest rates), and the strategy to manage public finance which has been underpinned by major reforms of the pension, health, education and taxation systems. But several weaknesses remain: the continuing external current account deficit, public finances (especially as debt servicing charges rise in years to come) and a weak labour market. In addition some of the reforms need to be taken further and to be better implemented, such as taxation and the management of health and pension funds.

Economic performance therefore remains vulnerable. Dynamic factors are at work which will greatly complicate the task of sustaining an effective economic performance in the future if steps are not taken now to deal with them. To avoid being blown off course will require a combination of prudent macro-economic policy as well as further structural and regulatory reform to address specific weaknesses such as slow progress in dismantling and restructuring the state-owned monopoly sectors, and unnecessarily burdensome regulations on business. The government's recent programme to promote the conditions for renewed economic growth identifies many of these weaknesses and proposes action to tackle them.

The strengths and successes of regulatory reform

Private sector activity has seen an enormous expansion, and foreign direct investment has boomed

The "shock therapy" deregulation of the economy in the early 1990s unleashed a wave of entrepreneurial activity. Thousands of new companies entered the market. Today the private sector generates 70% of GDP and employs 72% of workers. Trade liberalisation played a key role here. At the start of the transition, the government boldly made the Polish zloty fully convertible, and provided domestic firms with a competitive edge by setting the exchange rate well below the black market level to provide an export incentive. It also abolished the monopoly of state-owned trading companies on imports and exports. Poland became a WTO founding member in 1995.

Price deregulation was another key factor. Although many prices remain regulated, most prices were fully deregulated and began to operate as effective signals for a market-based system of resource allocation. In this context, a fundamental revision of the Rent Law in 1990 raised the availability and quality of trading space for companies, and broke the monopoly of the state-owned trading companies on this market.

One particularly striking example of the change to private enterprise was in road transport. This sector spontaneously reverted to private hands at the start of the 1990s (the intercity bus service (PKS) was partly privatised). Within a short time, thousands of small private transport enterprises were registered and took over from the state-owned companies.

Foreign investment interest in Poland was modest in the early 1990s, but gathered pace after 1995, encouraged by the reforms. Foreign companies have entered the market through privatisation purchases and green-field investments, each accounting for about half the total, and until recently aimed almost entirely at the domestic market. FDI in services has been linked to the privatisation of banking and telecommunications. Greenfield investments in manufacturing have been largest in transport equipment (passenger cars, trucks and buses) and the food and drink industry. Over 90% of this capital is from OECD countries, and its cumulative value in 2001 was estimated at USD 47.3 billion.

Better corporate governance has also helped the private sector to flourish, spurred by new laws and regulations. In particular, the Law on Accounting harmonised Polish standards with those of Europe, which greatly improved the transparency of bookkeeping (which helps to protect the interests of all stakeholders including the state and taxpayers).

The new Commercial Company Code of 2001, which aligned Polish with EU law, introduced a number of important improvements. It simplified the procedures for changing company status (restructuring, mergers, divestments and acquisitions). It banned stocks with multiple voting rights (with the exception of the State Treasury) and introduced non-voting shares. The powers of the supervisory boards and the prerogatives of shareholder meetings were increased. The rights of minority shareholders were strengthened.

An effective competition policy has helped to shape the new market economy

A market economy needs an effective means of stimulating competition and correcting and preventing anti-competitive behaviour. Early steps towards creating an effective basis competition policy were the 1990 Competition Law, and the foundation of

Table 4. **Structure of foreign direct investment (by sector)**

USD

Activities according to the European Classification of Activities (ECA)	1990-2000	1990-2000
Manufacturing:	**19 462.8**	**39.4%**
Transport equipment	5 167.7	10.5%
Food, drinks and tobacco products	4 961.9	10.0%
Services	**26 235.9**	**53.1%**
Financial Intermediation	10 392.7	21.0%
Transport, storage and communication	5 568.8	11.3%
Trade and repairs	3 962.6	8.0%
Construction	2 490.6	5.0%
Total investments over USD 1million	**45 772.0**	**92.7%**
Estimated investments under USD 1million	3 620.5	7.3%
Total FDI	**49 392.5**	**100.0%**

Source: OECD.

the Antimonopoly Office (AMO). AMO worked to create the market conditions for sustainable development. Its main concerns were the de-monopolisation of industry, large scale structural issues, control of natural monopolies and trade liberalisation. Its opinions about privatisation were usually followed by the government.

The government, as in many other areas, continued to develop and refine the policy. AMO was given consumer protection responsibilities in 1996, and renamed the Office of Competition and Consumer Protection (OCCP). The 1997 Constitution supports OCCP's work by stating that "restrictions on the freedom of economic activity can be imposed only by law and must be justified by an important public interest", and which obliged public servants to protect consumers against unfair marketing practices. The 2000 Law on Competition and Consumer Protection strengthened OCCP's formal independence (the OCCP President is now protected from discretionary dismissal), and gave it extensive investigative powers, as well as conforming the substance of Polish competition law with EU law.

The reform of the state has been a success

The creation of an almost entirely new framework of democratically accountable state institutions culminated in the adoption of a new Constitution in 1997. These changes were an essential building block for further reform: a starting point for the work which is still underway to restructure and improve public administration, and to introduce better regulatory practices. The rule of law has replaced the former authoritarian regime.

The scale of this enterprise cannot be overstated. Poland was subject to over 40 years of communism – though it had strong democratic roots in the pre-communist era – and a modern liberal democracy had to be created from scratch. The first goal to separate the executive, judicial and legislative powers was achieved without major problems. A genuinely independent judiciary was established, with a fully independent Supreme Court and a Constitutional Tribunal as the ultimate judicial recourse. The legislature also developed its own identity and a new relationship with the executive. While the government plays a key role preparing and enacting legislation, the parliament also has a strong influence: it initiates around a third of all laws passed.

Censorship was abolished and a free press quickly developed, making an important contribution to democracy. The country quickly adapted to a lively democracy, in which 11 free elections – presidential, parliamentary and municipal – have taken place since 1989.

Nearly all the basic laws that govern the structure of the state and the relationships between its component parts have been substantially changed or amended. The approach has been pragmatic and somewhat *ad hoc*. The government has made successive changes in response to the challenges of the time and to consolidate improvements (for example the Parliamentary election law was amended four times to get the election process right and to adapt to administrative changes).

Restructuring and reforming the public administration has been tackled, and a comprehensive administrative framework and principles are now in place

The central administration of government has also been substantially overhauled. A series of laws from 1996 onwards promoted a major restructuring of the centre of government. The objectives were to adjust the centre to local government devolution, reduce a large and inefficient bureaucracy, remove overlap of responsibility between ministries, create horizontal structures to facilitate co-operation and the resolution of differences, change procedures to improve the quality of legislation, and create mechanisms to promote harmonisation of laws with those of the EU. Relevant subsidiary bodies were created in the process, for example the Committee for European Integration which is responsible for co-ordinating the process of integration with the EU.

The Civil Service Law of 1998, which covers central and local government administration, created the civil service corps, defined the rights and obligations of civil servants, created a central office of the civil service, and set out transparent and competitive rules for career progression. In the short term, though, its implementation has created some bottlenecks in the recruitment of high-level officials.

Big efforts have been made to improve regulatory quality

To complete the broad strategic reforms of the state and public administration, the government also embarked on more specific reforms to improve capacities to produce quality laws and regulations. Internal procedures for preparing draft laws have been improved through the involvement of the Government Legislation Centre (which co-ordinates legislative work), and the Legislative Council (which advises the Prime Minister). In September 2000 the Regulatory Quality Team was established as an advisory body to the Prime Minister, taking on as one of its first tasks elaboration of the RIA system. Since then, the Team has taken responsibility for advocating further regulatory reform (a role that was partly played by the now defunct Debureaucratisation Task Force). The Government Centre for Strategic Studies will also participate in challenging the findings of RIAs presented to the Council of Ministers by proponent ministries.

In 1999, the government adopted a document "A Conception of Medium-Term Economic Development of the Country until 2002", in which it committed to the tasks of ensuring high quality new regulations, eliminating ineffective and redundant laws, adopting international agreements into the domestic regulatory system, and increasing the transparency of public activities.

Restructuring and reform of the financial system has been a great success

Financial services, crucial for the country's economic development and to a positive entrepreneurial climate, had to be more or less created from scratch. Structural and regulatory reforms have been essential to this process. The transformation was greatest in the banking sector. The 1993 Law on Financial Restructuring of Enterprises and Banks, and the 1998 National Bank of Poland (NBP) Act, together with a strong supervisory framework built up by the NBP encouraged banks to clean up their balance sheets and significantly improve their prudential ratios.

Most of the state-owned banks have been privatised (with the exceptions of the largest retail bank, PKO-BP, and BGZ SA). Foreign investors were encouraged to participate so that the banks could benefit from capital and know-how. Today Poland has one of the most internationalised banking sectors of the region. Thanks to the large foreign presence, strong competitive pressures and sound prudential supervision, the Polish banking system is also among the strongest in the region, which proved itself by emerging unscathed from the Russian crisis of 1998-1999.

The creation of a modern stock market was another major achievement of the decade. The 1991 Law of Public Trading in Securities and Trust Funds, and the creation of the Warsaw Stock Exchange in the same year set the scene. An independent and legally strong Securities and Exchange Commission to regulate the new market was also set up. The Law created an appropriately stringent environment for stock trading, with emphasis on transparency and shareholders' rights. The Polish stock market therefore took off from a strong base – boosted by a number of IPOs. It has progressed steadily and in 2000 had more than 200 listed companies with a market capitalisation more than 20% of GDP.

A modern insurance sector has also been established. The 1990 insurance law (with subsequent amendments) created a proper legal and institutional environment, and a specialised regulator, the State Office for Insurance Supervision, was set up. The insurance market was opened to competition, and some 30 general insurance and 30 life insurance companies have entered the market, including a strong international presence, which has stimulated competition. However in contrast to banking, a major state-owned player (PZU) still dominates both general and life insurance. Although 30% of the shares in PZU have been sold, the sale of the state's remaining stake has been slow and, most recently, subject to extensive political discussion.

Finally, a new market in pension funds took off with the changes in pension policy. As with the other financial sector developments, it was based on another new law – the 1997 Law on Organisation and Operation of Pension Funds – and a new regulator – the Pension Fund Supervision Office (UNFE), responsible for the legal and organisational aspects of pension fund operation.

Table 5. **Selected legal and regulatory developments in Poland**

1989 – First free Parliamentary elections – Beginning of the Reform of the State

Reinstatement of the system of decentralised local government on the level of *gmina* (municipality), first democratic local general elections
Essential changes in the State Budget programming, separation of the State budget from the local budgets
Law against monopolistic practices and establishment of the Antimonopoly Office
Tax reform, introduction of income tax for all individual tax payers

1992 – Adoption the so-called "Small Constitution" (*Constitutional Law on the Relationships between the Legislative and Executive Powers and on Local Self-Government*)

Tax reform continued – introduction of value-added tax (VAT)
Adoption of the law on the Supreme Administrative Court
Law on Public Procurement, establishment of the Public Procurement Office

1994 – Application for accession to the European Union – Proceeding with Clear Objectives

Law on the Organisation and Rules of Procedure of the Council of Ministers and on the Sphere of Competence of Ministers "Law on Organisation"
First Civil Service Law
Law on Privatisation and Commercialisation of State-owned enterprises
Introduction of mass privatisation, establishment of the Public Enfranchisement Funds

1997 – New Constitution – Enhancing the Policy and Regulatory Management Framework

Reform of the State system, adoption of additional levels of territorial local government: *powiats* (counties) and *voivodships* (regions)
Law of the General Health Insurance
Law of the Social Insurance System
Law on the Civil Service
New Business Activity Law
New Commercial Company Code
Establishment of the National Registry System;
Law on establishing the Polish Agency for Enterprise Development
Law on the conditions for admissibility and monitoring of publzic aid for entrepreneurs
Freedom of Information Law

Source: OECD.

The challenges confronting future regulatory performance

The pace of change has been enormous, and there is now a pressing need to address the quality of human resources harnessed to the reform effort

Change has been a necessary feature of the Polish landscape for over a decade. If anything the pace has accelerated in the last few years. For example 1999 saw the simultaneous introduction of four fundamental social reforms – public health care, social insurance, administration and education. This has put a huge strain on the human resources deployed to draft new laws and regulations, and staff the new regulatory and other offices that have been created. Actual performance has, perhaps not surprisingly, lagged behind the leap forward in legal and organisational structure. Not all the objectives foreseen in the new blueprints have been met. For change to be effective, people, processes and institutions need to be "up to the job".

In particular, the Polish public administration still faces important challenges, and has some way to go before it can be considered a thoroughly effective and modern civil service. Issues holding it back include inadequate remuneration, poor management (not least poor financial controls), some overstaffing, low skill levels, and lack of adequate training. The Civil Service Law clearly envisages a dedicated, well-educated, independent and ethical career civil service. But changes here are happening slowly, partly because some decision-makers are still in a difficult transition away from an interventionist culture. Poland as well as other OECD countries have found that the progression of a new generation of managers supports this transition.

Cases of nepotism and corruption are still visible in some areas. According to Transparency International there is some evidence that unethical behaviour is spreading. Public opinion surveys indicate that Poles are increasingly convinced of this. The World Bank has given Poland 4.2 out of 10 for corruption (10 means there is no corruption), and has provided examples of areas that are vulnerable to corruption. The EU Commission has also been critical.

The legal and institutional framework can ultimately only be as good as the people who operate it so this is a major and disturbing weakness. The government has taken important steps to address the issue and enhance accountability, including ratification of the 1990 Council of Europe Convention on money laundering and the 1997 OECD Convention on bribery, as well as the creation and strengthening of an Ombudsman (Commissioner for Civil Rights Protection).

But action needs to be sustained and developed on many different levels, not least training and action to encourage culture change. Resources also need to be adequate for important tasks such as competition policy communication. As part of the problem stems from laws and regulations that allow too much discretion, this regulatory weakness should be vigorously tackled. By giving citizens the right to an explanation of public authorities' decisions, the recently adopted Freedom of Information Law should provide a huge boost to accountability.

There is an equally pressing need to improve the quality of regulation through better administrative tools and more consultation

The government's policy is to eliminate ineffective and redundant primary legislation. The massive effort to transpose EU legislation into Polish law has been especially helpful in

this respect (although the speed of adoption of the EU acquis, which is huge, has generated quality problems). The government has also run a programme to codify the laws, and has a policy to reduce regulatory burdens on industry, particularly Small and Medium-sized enterprises (SMEs). The new Constitution required a comprehensive review of the legal framework. Poland has also developed administrative and governmental procedures to improve internal communication on draft regulation, and controls on the quality of legal text.

But until recently there has been much less emphasis on other aspects of quality. The creation of new rules and their codification has taken precedence over cost-effectiveness, elimination of duplication and overlap and effective implementation. All these issues will eventually need to be addressed for a high quality regulatory environment. A place to start is to increase the quality of justification of new regulations, and the involvement of affected parties. But this is easier said than done. It involves developing and enforcing a wide range of practices, from standardised processes to make and change regulations, the use of RIA, systematic consultation with interested parties (all of them), plain language in drafting, communication to make rules understood and more accessible, and effective implementation and compliance. Poland shows recent progress in the development of these tools. However their integration into the administrative culture and consistent implementation across the government is still a challenge.

Effective public consultation is particularly important. It gives stakeholders the opportunity to make an active input to the shaping of new rules, so that these are better adapted to circumstances. It also promotes their "ownership" of the rules, and hence better compliance. To be fully effective consultation must be systematic and routine, and it must extend to all important stakeholders. The adoption of the Freedom of Information Act in September 2001 was an important step in the right direction. Provisions of the new law make consultation a more common and standardised process from the previous practice of consulting some, generally traditional, groups (such as the chambers of commerce, unions, and the church) but leaving out other important interests. With the new tools provided by the law, such as the Public Information Bulletin (when launched) and the use of an Internet-based platform, communication with society should be considerably enhanced.

The use of Regulatory Impact Analysis (RIA) is an excellent way to ensure that regulations are of the highest quality, as it combines good habits of consultation with a rigorous assessment of the impact of prospective rules. It involves making a clear and balanced assessment of the costs and benefits of a new rule, a challenging process requiring a big investment in training and new practices if done well.

After some months of development, the government introduced an RIA system in late 2001. The Rules and Procedures of the Council of Ministers as well as the Law on Organisation were amended to incorporate RIA in the rule-making procedures. From now on, proponent bodies need to annex an RIA to the "justification report" necessary for the approval of all the acts by the Council of Ministers, as well as ministerial acts. The Government Legislation Centre has been assigned the task of overseeing the RIA process. The Government Centre for Strategic Studies (an independent advisory body to the Prime Minister) will also play a challenge role for RIA quality. It will provide a second RIA for regulations with an important long-term impact on social and economic development, and when the Prime Minister deems it necessary. These measures are encouraging though it is too early to make any judgement of their neither effectiveness nor judge how the two RIA

assessments will be reconciled if major discrepancies exist. As in the case of public consultation, effective implementation of the system will be vital to secure success.

Other important actions to tighten up regulatory quality include the need to draw back from the current proliferation of detailed regulations and prefer approaches based on codification and organic or leading laws, and to work on simplifying and standardising language and texts. The Legislative Council criticised performance on both of these issues in a recent report.

Implementation, enforcement and compliance must not be neglected

Implementation, enforcement and compliance are also critical to success. Laws and regulations remain an "empty letter" without this –praiseworthy statements of intent on paper that have little connection with real life. This issue remains a big structural weakness. Ambitious and soundly based reforms such as the overhaul of health care have suffered from mistakes and inefficiencies in implementation. The devolution of powers to local government has not been effectively followed through. The efforts to help business with a national business registry and improvements in the tax regime have taken off but require completing.

A large part of the solution lies with efforts to tighten up on regulatory abuse – excessive and poorly applied administrative discretion, and corruption. Another big problem is the delays in court proceedings. The judiciary is inefficient and under-financed. The increasing number and complexity of cases have led to serious delays, especially in Warsaw (cases may take several years to resolve). This could foster bribery and corruption. Steps have already been taken to reduce backlogs (such as the establishment of 300 new district Courts, part of the local courts), facilitate business registration (with the Business Registry System in operation since 1 January 2001) and improve access to data on penalisation for the purposes of court proceedings (with the Penal Registry System in operation since June 2001). These will, however, need to be reinforced.

Implementation also means paying attention to secondary legislation that needs to be enacted without which the primary law is not much use. Laws must in principle be submitted to Parliament together with the major implementing regulations. In practice however, secondary regulations can be adopted at a later stage. For instance, where a new law replaces an old one, Parliament typically maintains the secondary regulations of the previous law whilst new regulations are developed by ministers. When developed, the new implementing regulations are not presented to Parliament. An important example of delays in the legal implementation process is the need to continue enacting the full range of ordinances to give effect to the Telecommunications Law passed by Parliament in 2000.

The strength of the new institutional framework needs to be tested

Alongside laws and regulations, the institutional framework is the backbone of the reform effort. The institutions to drive and co-ordinate reform seem now to be in place. The centrally controlled law-making mechanism, which has been set up under the Law on Organisation (which includes the Government Legislation Centre and the Legislative Council), is a big step forward in improving regulatory quality. However, time, resources and effort are needed for its success. Experience from other OECD countries shows that the introduction of a modern regulatory management system needs constant adaptation and a strong political will. As the process takes root, higher standards can be met and

Box 1. **Main regulators in Poland**

Since 1997, the **Energy Regulatory Authority** (ERA) regulates the activities of energy enterprises in accordance with the provisions of the Energy Law and the energy policy of the state. According to the Constitution, the Regulator is not authorised to issue generally binding acts. The President issues administrative decisions, which are subject to appeal proceedings in the Antimonopoly Court. The Minister of Economy monitors ERA activities.

The **Office of Telecommunications and Posts Regulation** (URTiP) regulates the telecommunications and postal sectors. It replaced the Office of Telecommunications (URT), created in January 2001, in April 2002 (as part of the central government organisational changes under the March 2002 Act). It has taken over all the tasks of the URT including frequency management and the monitoring of compliance with electromagnetic compatibility requirements. URTiP has a consultative and advisory body called the Telecommunications Council. URTiP also takes over control of the postal market and tasks related to granting permission for the performance of economic activity in the postal field (which had previously been with the minister responsible for the postal sector). When the new Postal Law is adopted URTiP will have additional regulatory tasks flowing from the Law including control over compliance with the Law's provisions on the delivery of universal postal services, monitoring the accounting separation for these services, determining whether universal service prices are cost-oriented, and monitoring the accessibility and quality of universal services. The Minister of Infrastructure, who covers posts and telecommunications, is in charge of monitoring URTiP's activities. Administrative decisions issued by the URTiP President are subject to appeal proceedings in Antimonopoly Court.

Financial Sector Regulators are subordinated to the Minister of Finance. Recently the government has undertaken to abolish some of the existing institutions and replace them with a single supervisory authority. Between March and December 2002, the State Insurance Supervisory Office, the Pension Funds Supervisory Office and the Health Insurance Supervisory Office will be merged into the **Supervisory Commission for Insurance and Pension Funds**. This body will work in co-ordination with the Securities and Exchange Commission and the Banking Supervisory Commission.

The **Office for Competition and Consumer Protection** (OCCP) is a central administrative body supervised by the Prime Minister directly. OCCP enforces the Competition Law virtually to all sectors of the economy and in the areas of banking, energy and telecommunications competence is shared with sectoral regulators. Administrative decisions issued by the President of the Office are subject to appeal proceedings in Antimonopoly Court.

In January 2002, a major restructuring of administration was launched. The following institutional changes will take place before the end of the year:

- 17 state administration bodies, 12 service offices to the state administration bodies, and 4 agencies are to be abolished.

Box 1. **Main regulators in Poland** *(cont.)*

- 2 agencies, the Polish Agency for Foreign Investment and the Polish Information Agency are to be merged; and
- 4 new state administration bodies will be created.

Source: Government of Poland, February 2002.

improvements made. In the case of the Parliament, the process is at an early stage. The role of its Chancelleries should be enhanced.

More generally question arises as to whether the most appropriate institutional framework has now been established for a market-based economy. Is there a need to improve the framework? Problems which may exist include overlap of responsibilities requiring some rationalisation, staffing as well as independence and accountability issues. Recent reforms, however, are a positive step towards a more efficient and focused institutional architecture.

One particular set of relationships that needs monitoring is the competition authority (OCCP), the sectoral regulators and the relevant Ministries. The OCCP has played a crucial role in the development of the market economy and in the major structural and reform programmes. As new sectoral regulators take up their role, they and the OCCP need to ensure that decisions and rules reinforce each other.

The position of the OCCP, to support and promote competitive markets, needs to be strengthened. This strength will be needed in the challenges ahead relating to state aids (for example in the coal sector). Opportunities have been missed to promote competition in reforming infrastructure industries (for example in the timid liberalisation of postal services, and the continuing monopoly granted by the Telecommunications Law to TPSA for international services). More resources are needed at the Antimonopoly Court, too, to reduce delays.

By the same general token the sectoral regulators need attention. Poland has been setting them up since the early 1990s, and the EU harmonisation programme has accelerated the process. The terms of their relationship with the OCCP vary, which can be confusing and potentially inefficient. Independence and power – provided there is effective accountability – is good, and helps to avoid capture by the political process and by the industry that is overseen. The regulators are set up to be independent but their powers are heavily circumscribed, with the Ministry retaining the lead authority for making regulations (there is a constitutional constraint on their ability to issue new regulations).

The decentralisation process and local government institutions need special attention

Devolution of tasks performed by the central government to local government was one of the major changes that took place in the reshaping of Poland's administration. Today, over half the tasks formerly performed by central government appear to have been devolved. This is in very sharp contrast to the communist period when everything was decided in Warsaw, although Poland does remain a national country with a uniform legal

system. There are now 2 489 municipalities (gminas), 315 counties (powiats), 65 towns with powiat status and 16 regions (voivodships) – a vast improvement on the previous (and toothless) structure of 49 voivodships, but probably a few too many for efficiency and for financial comfort (financial resources are tight relative to the number of tasks).

The practical application of devolution does not appear to have received the same attention as administrative issues at the centre of government. In principle, much of the framework of devolution is sound. A dual system has been established in which the regional elected governments cohabit with a regional "prefect" appointed by the Prime Minister. Constitutionally, national law has primacy over local law and all citizens can require a judicial review of a local law. The Ministry of the Interior oversees the work of the prefects and hence the regulatory process at the regional government level.

But the system is clearly struggling to work effectively in practice. Concern has been expressed at the way regulations are developed and applied. In 2000 alone, 13 637 acts were published in the regional legal gazettes. The Ombudsman has drawn attention to the "lack of transparent legal regulations and efficient instruments of supervision of local government authorities" and has noted that "the changes brought to light problems caused both by inconsistency of the provisions regulating the powers of different levels of local government and poor co-operation between the State administration and local government bodies".

The World Bank has also raised questions about the number of governments operating in the same areas, which complicates lines of responsibility and reduces transparency. Excessive discretion and lack of adequate controls over the implementation of framework laws as well as the design of local regulations (in areas such as zoning, licences and permits for economic activity, contracts for construction works, goods and services, property rent controls and tariffs for public services), create unnecessary burdens and can foster corruption.

Some recent initiatives to improve matters should help. A 2001 initiative to adjust court jurisdiction to the administrative borders of the new regions should improve co-operation between central and local authorities. The OCCP has intervened to promote competitive markets at the local level, with recent cases focusing on exclusive agreements for cable TV services, the creation of local monopolies for waste collection, and abuses of funeral service provisions.

But a more systematic plan is urgently needed to improve local regulatory quality, and address the many issues that devolution has brought in its wake. Basing local finances more on local taxes and less on central government transfers could help to improve the accountability of local government. However a careful distinction needs to be drawn between programmes of a national character that are delivered at the local level (such as medical care, education, old age and social assistance) and other more traditional local government responsibilities (such as water and waste services, roads and parks). Among the first group the current system of central government transfers and supervision helps to ensure horizontal equity while for the second group, local financing allows for a better alignment between services provided and local preferences. Despite these important distinctions, initiatives are needed to raise competence and skills at the local level, and better supervision of local administration needs to be put in place. In short, action is needed urgently to improve the quality of local regulation.

Vigorous private sector activity is a cornerstone of the economy: to keep this up the environment for SMEs needs further improvement

Vigorous entrepreneurship is held back by a number of remaining regulatory obstacles, despite the government's clear intention to improve the environment for SMEs through major initiatives. These have included the 1999 Business Activity Law, which thoroughly reformed the legal framework for enterprises by enshrining principles of freedom to undertake and conduct business, equal rights of entrepreneurs, fair competition, consumer rights protection and fair practices in trade.

The new law also rationalised the licensing and permit regime. The number of areas of activity subject to licences was reduced from around thirty to eight (with some tightening of entry restrictions for the professions that remained subject to licences). In fourteen of them the obligation to obtain a licence was replaced with the obligation to obtain a permit (which is automatically given if a business satisfies the conditions). In eleven cases, licensing was abandoned completely. Administrative discretion was reduced in consequence. However, some anomalies remain. For instance, there are three separate bus transport permits (for regular, irregular and occasional transport).

It is too early to assess properly the impact of recent measures, such as the establishment of the Polish Agency for Enterprise Development, to improve the business environment. The real measures of success will be continued growth, and exports. But some misgivings arise, for example specific regulations, which obstruct staff recruitment and retention, and excessive discretion in the allocation of funds, which is distorting effective competition. Tax regulations are still complicated. "Red tape" remains an issue.

Some sectors need an adjustment, development or radical overhaul of regulation

Achievements should not obscure the need to adjust – or even if necessary overhaul – the regulatory framework in some parts of the economy. The regulation of the pension fund market needs attention. Early strong limitations placed on the kinds of investment that funds could make are necessary to get the market off to a sound start. However these were meant to be relaxed gradually and this has not happened. The market is now maturing and consolidating, which is essential for it to stay on a sound footing. Unfortunately excessively restrictive regulation serves to reduce returns, the attractiveness of the pension funds and potential benefits of reform. They are no substitute for good corporate governance practices, and have the effect of denying an important source of capital to a large subset of firms.

Corporate governance would be helped by a new bankruptcy law. Serious delays in judicial procedures have allowed some enterprises to try and delay repayment of their trading liabilities, raising the cost of doing business. Also, several important companies are immune from the current bankruptcy law (the railway company PKP for example) and some are protected by government orders (for example the steel company's arrears to the public pension system). These restrictions not only have a negative impact on related companies and trading partners, but affect the whole economy.

Regulatory failures have held back a necessary and rapid expansion of the intercity road network. Despite early efforts to move forward – motivated by the virtually complete lack of motorways – only about 260 km of motorways have been built since 1990. A fundamental error turned out to be the belief that the motorways would be built entirely by the private sector. In fact just 60 km of toll motorway has so far been built, partly because

the Agency for Motorway Development has failed to enforce licences to build. Companies are demanding government participation, which has been enabled through the 2000 amendment of the Motorways Law allowing public-private partnerships.

A review of attitudes to transposing EU laws may be desirable. Having to do this for accession to the EU has been a great boost for reform so far. But in some cases it does not appear to be clearly understood that the EU directives represent the lowest common denominator of necessary legislation, and not necessarily best international practice. In other words many EU countries may be going further and faster, and these countries will be better placed to benefit from EU liberalisation and the single EU market. The EU "acquis" is not enough. In some other cases (such as electricity liberalisation) it would be beneficial for Poland to consider implementing at least the minimum *before* accession so as not to be competitively disadvantaged. The bundling of laws, whose only connection is the EU accession agenda, in order to speed up their adoption does not help transparency.

Last but certainly not least, the remaining state monopoly sectors need a much more courageous approach to liberalisation

Although the private sector now generates 70% of GDP, a substantial share of firms and productive capacity remains either fully or partly state-owned. While privatisation has so far often compensated for a relatively weak legal environment through strategic partnerships with privatised firms, the sheer volume of companies still in state hands requires the adoption of a much faster approach. It is almost impossible for the Treasury to provide adequate corporate governance and assure effective control of the 3 900 or so state enterprises and companies with a Treasury share in its portfolio as would a private owner. Some uncomfortably large state-owned and controlled companies continue to dominate their industry. Privatisation of some of them is still to be completed (for example in the insurance sector).

Many state-owned companies continue to benefit from significant advantages as compared to those in the private sector. In particular, many of these firms continue to accumulate substantial tax and social security arrears which are either not being collected or forgiven. And many such firms benefit from implicit or even explicit state guarantees on their debt, while the recent slowdown in the privatisation process serves to reduce competitive pressures.

Liberalisation of the state sector is perhaps the most incomplete element of the reform agenda to date. In many cases only timid and inadequate reforms have been engaged. Many large state-owned sectors (such as post and gas) received little attention in the liberalisation and deregulation wave of the early 1990s for a number of reasons, including their perceived strategic position in the economy, the social consequences of major change for industries that employed large numbers of workers, and (in some cases) their sound finances. Difficult but important decisions, essential for completing the market economy, were delayed.

But in the last few years the need to meet conditions for EU accession in which the importance of competition issues was stressed, and the exploding indebtedness of some sectors such as hard coal which undermined the whole economy, galvanised the government into action. Restructuring, privatisation, regulatory reform and liberalisation are being tackled, with varying enthusiasm. The government's recent programme to

promote economic growth includes proposals for a more radical approach to the restructuring of the energy and some other sectors.

The *energy sector* has already seen a substantial government withdrawal through privatisation, but this process and the closely linked issue of restructuring is flawed and far from complete. In at least one important case (oil refining) the approach to privatisation placed insufficient weight on achieving the most effective new structures for a competitive market. Thus the government created a vertically integrated giant in the oil refining business – PKN Orlen – by combining Poland's biggest refinery with its largest distribution network, as well as storage. This means that the sector will need close surveillance by the OCCP over the foreseeable future.

In coal, gas and electricity stronger efforts are being made to ensure that the structure of the industry is right for competition *before* privatisation or at least that the assets sold are appropriately desegregated. But even here progress has been slow and some of the plans flawed. As noted, the government now seems more determined to pursue a stronger strategy.

Box 2. **The state-owned sector in Poland**

By early 2002, Poland had 2 100 state enterprises, about 700 of which are presently subjected to insolvency and clearance procedures. Out of the 1 800 (commercialised) companies with the Treasury share:

- About 500 companies belong exclusively to the Treasury,
- In 108 companies the state owns a majority share (more than 50%),
- In 489 companies the state owns between 25 and 50% of the shares, and
- In 725 companies the state owns less than 25% of shares.

According to the new economic strategy "Entrepreneurship-Development-Labour" announced in January 2002 the Government plans to complete ownership structure transformations by the end of 2005 aiming at achieving a similar structure of a EU country. It is envisaged that the state will continue to control Poland's infrastructure and networks such as airports, seaports, railroads, and electric energy and gas grids as well as public utility services and lotteries. The legal and organisational grounds for further restructuring of state-owned enterprises will be drafted by July 2002. The government also plans to set up a Restructuring Fund in connection with the privatisation process; for example, increasing the market value of an enterprise and introducing public-private partnerships. Revenues from privatisation should support new infrastructure projects.

Source: Government of Poland, January 2002.

An ambitious programme is in place to restructure the hard coal sector and bring it closer to international competitiveness standards but there is some way to go, including further mine closures. In electricity, generation and distribution have been separated from transmission and system operation, but these last two functions remain bundled with large trading activities, with the effect that the company in charge retains a dominant position in the whole market. Future privatisations will need to avoid any excessive reaggregation of generation and distribution. It is not yet clear whether the stranded costs created by long term power contracts that currently dominate the market and prevent effective competition will be successfully handled. The natural gas sector is the least advanced. A single vertically integrated company is still in place. The restructuring plans look good on paper but have yet to be implemented.

Privatisation is still very partial, and some of the plans do not envisage full privatisation, though steps have been taken to distance the government and give a stronger commercial orientation to companies it controls. The state has withdrawn most from the oil sector, with the largest company now less than 30% in state hands. Privatisation of hard coal mines has been delayed by the sector's parlous financial state being the reason for delay. The planned privatisation of the first profitable mine in 2001 has not yet taken place. Most of the electricity sector remains in state ownership, and partial privatisation is still on the drawing board for natural gas, which remains wholly under state control.

Liberalisation and reform of the regulatory framework also needs to be completed. In all the energies bar oil, there is a need to dismantle impediments to free trade (for example discrimination against electricity and gas imports). In the sectors with natural monopoly characteristics – electricity and gas – greater care is needed in developing a new regulatory framework that will be effective in managing the residual monopoly elements, and in ensuring a transition to competition that allows new entrants full scope to exploit the new markets. The deregulatory spirit of the 1990s is not appropriate in this context – careful reregulation is necessary in such areas as tariff control, long-term contracts, and third party access to the networks. The new sector regulators need adequate powers and staff to oversee these issues. The government has not neglected this important programme, but needs to go further and faster.

The *postal sector* remains one of the most monopolistic in the economy with the incumbent retaining virtually 100% of the market in respect of letter post services of up to 2 000 grams in the context of universal service. The government has been reluctant to liberalise the sector significantly and free it of state control, even to the point of delaying adoption of a new postal law to bring it line with the modest requirements of the EU. The concern about maintaining a quality universal service is not warranted in the light of the experience of some other OECD countries, which have fully liberalised.

The *telecommunications sector* remains monopolistic. The incumbent still dominates fixed line telephony and is scheduled to keep its exclusive rights in international services until the end of 2002. The effect of limited competition and weak regulation so far is that Internet connection charges are among the highest in Europe, and the telecommunications infrastructure (especially in rural areas) is highly undeveloped. There is up to a year's wait for a telephone connection in some areas. As with oil refining, restructuring and privatisation has been driven by revenue raising considerations rather than the needs of competition. Much further work needs to be done to tighten up and develop the regulatory

framework to allow competition to flourish, including a new interconnection regime, price regulation aimed at operators with significant market power, the introduction of number portability and a new regulatory framework for universal service. The new regulator needs the authority to implement this new framework.

The *steel industry* is in poor condition, despite restructuring efforts throughout the 1990s, and a significant modernisation of the largest steelworks. The product mix still includes a high share of semi-finished steel products, while high value added steels are not produced at a sufficient level. As in other parts of the world, the sector currently faces huge losses and debts. Privatisation has been delayed until recently. At present, negotiations are carried out for an "en bloc" privatisation of the four most important steelworks.

Reform of the *railways* is in better shape though until recently it had proceeded slowly. This changed when the finances of Polish State Railways (PKP) – a monopoly state company with the largest number of employees (200 000) – started to worsen in 1998 as a result of the difficulties experienced by major customers, among them the hard coal and steel industries. A first step was commercialisation (into a commercial state-owned corporation) followed by the gradual restructuring of PKP into operational companies under a holding structure engaged in passenger and commodity transport, and some liberalisation which started with freight transport.

Conclusion

Regulatory reform is central to the economic and social transitions underway in Central and Eastern Europe. For Poland and its neighbours reform is not just about deregulation, but also the creation of new regulatory systems conducive to good governance and the establishment of new relationships linking citizens, the state and the market. It involves the dismantling of central-planning institutions and laws; the building of new regulatory regimes; and the strengthening and rebuilding of institutions and capacities dormant from the past, to lay the basis for co-operation, power-sharing and decentralisation in a democratic society.

The efforts to turn around the Polish economy and society since the fall of communism have been massive and have already reaped results. The country is unrecognisable compared to what it was in 1989. It is governed by democratic institutions and the rule of law. The bold programme of economic transformation launched in 1990 has yielded a remarkable growth in the economy, based on productivity gains. The important message is *not* to let up at this stage on further work to improve the market economy that has been so painfully created. This means more effort, in particular, on implementation of the regulatory reforms that have already been made. The effective implementation of new laws can make a crucial contribution to tackling weaknesses including corruption, and management of the remaining large monopoly sectors. Reform "fatigue" must be avoided.

Important links exist between regulatory reform, entrepreneurship, structural change and employment. The more the regulatory environment can promote the further development of SMEs, the easier it will be to promote further necessary structural changes and the better for employment prospects and a reduction in the informal economy. As experience has shown in many countries, reform that transforms the regulatory environment is one of the best policies to improve economic growth and social welfare prospects.

*PART II**

REGULATORY POLICIES AND OUTCOMES

* The background material used to prepare this report is avaliable at: *www.oecd.org/regreform/backgroundreports*

PART II

Chapter 2

REGULATORY GOVERNANCE*

* For more information see: "Background Report on Government Capacity to Assure High Quality Regulation" at *www.oecd.org/regreform/backgroundreports*

Background

The groundwork was laid in the 1990s, creating a robust platform for further work to enhance regulatory quality

As in other countries of Eastern Europe, Poland's transition to a democratic market economy has involved a challenging process of fundamental regulatory change, from deregulation and privatisation to the creation of new regulatory systems capable of promoting effective governance. The transformation of the regulatory landscape began in earnest with the government which came to power in 1989, spurred by a crisis that threatened to engulf the country in economic chaos. It developed pragmatically on five fronts: the democratisation of state institutions, economic reforms to establish a free market economy, the devolution of powers to local government, the objective of joining the EU, and the reform of the state's administrative and regulatory capacities.

Rapid democratisation began with the first free Parliamentary elections and the reinstatement of Parliament's upper chamber in 1989, followed by the first democratic local elections in 1990. These changes went alongside economic reforms which centred on a "shock therapy" programme of deregulation and liberalisation, including a cut in state subsidies and the removal of most price controls. The antimonopoly office (precursor to today's competition authority, the OCCP) was established in 1990 and played a key role in promoting the economic reform agenda. Devolution gathered pace in 1991 when local budgets were separated from the central state budget. 1991 also saw the start of an ambitious fast track course to join the EU (a formal application was made to join the EU in 1994), which required a fundamental adaptation of Polish legislation to the structure and content of the EU legal framework. Reshaping state institutions and processes – a massive undertaking covering fundamental issues such as a new Constitution and law-making process – also began. Some institutions, such as the Tribunal of State were revived, and others, such as the Constitutional Tribunal and the Ombudsman (Commissioner of Citizens' Rights) were created.

These reforms were further developed in the second part of the 1990s, and beyond. (Part one, and the trade and sectoral sections of Part two of this report cover the economic reforms.) The State Economic Administration Reform was launched in 1996 through a Law on Organisation. This transformed central government organisation, including an adjustment of its relationship to the newly empowered local governments, the reduction of a large and inefficient bureaucracy, removing overlap in the competences of ministries, the creation of horizontal structures to promote interministerial co-operation (including on regulatory management), procedural changes to improve the quality of legislation, and the creation of mechanisms to harmonise Polish law with EU law. Further initiatives including institution building followed to improve governance in the public administration. A new Constitution was ratified by national referendum in 1997. This had two major impacts on the legal order. It led to a cataloguing and clarification of the different legal instruments,

eliminating major inconsistencies in the sources of law. It also triggered a review of existing laws: hundreds of laws were replaced, removed or redrafted. The 1998 Civil Service Law paved the way for creation of the civil service corps, defining the rights and obligations of civil servants, as well as a management and career progression structure.

The government has confirmed its formal commitment to the principles of regulatory quality: their implementation needs more work

The essential groundwork of successive governments through the 1990s and beyond means that today Poland has many of the policies and institutions in place to continue the reform process and promote quality regulations. It is moving towards OECD good practices, though there is a need for further improvement.

Poland committed itself to OECD regulatory reform principles (set out in the 1995 Recommendation for Improving the Quality of Government Regulation) in June 1999 with a government paper "A Conception of Medium Term Economic Development of the Country until the year 2002". This committed the government to ensuring high quality new regulations, eliminating ineffective and redundant laws, adopting international

Box 3. **Good practices for improving the capacities of national administration to assure high quality regulation**

The OECD Report on Regulatory Reform, welcomed by Ministers in May 1997, includes a co-ordinated set of strategies for improving regulatory quality, many of which were based on the 1995 Recommendation of the OECD Council on Improving the Quality of Government Regulation. These form the basis of the analysis undertaken in this report, and are reproduced below:

A. BUILDING A REGULATORY MANAGEMENT SYSTEM

1. Adopt regulatory reform policy at the highest political levels
2. Establish explicit standards for regulatory quality and principles of regulatory decision-making
3. Build regulatory management capacities

B. IMPROVING THE QUALITY OF NEW REGULATIONS

1. Regulatory Impact Analysis
2. Systematic public consultation procedures with affected interests
3. Using alternatives to regulation
4. Improving regulatory co-ordination

C. UPGRADING THE QUALITY OF EXISTING REGULATIONS

(In addition to the strategies listed above)

1. Reviewing and updating existing regulations
2. Reducing red tape and government formalities

1. OECD (1997), "Regulatory Quality and Public Sector Reform", in *The OECD Report on Regulatory Reform: Thematic Studies*, Paris.

agreements into domestic regulatory system, and increasing the transparency of public activities. Regulatory reform policy was further developed in a September 2000 government resolution "to achieve sustainable development, to increase the competitiveness of the country and to improve the quality and transparency of government". A key output followed in September 2001 with the legal implementation of a Regulatory Impact Analysis (RIA) policy. It has been incorporated into the law-making process through appropriate amendments to the Rules and Procedures of the Council of Ministers and the Law on Organisation, which entrusted the process of co-ordinating RIA implementation to the Government Legislative Centre.

Practical implementation of regulatory quality principles has so far been strongest in the commitment to eliminate ineffective and redundant legislation. A number of policies have helped with this: the massive effort to transpose EU law, the Ministry of Justice's programme of law codification, the Ministry of Economy's policy to reduce regulatory burdens on industry, especially SMEs, and the revision of laws needed for the new Constitution.

But other aspects of regulatory quality have not yet been given the same push. In particular, there is a need to implement the policy on RIA effectively. Quality standards need to be specified, the reviewing institutions need to be strong enough to act as credible advocates of better regulation, and the relationship with competition and devolution policies needs attention. The focus on new regulation also needs to be balanced by the need to improve the quality of existing regulation.

Institutions and mechanisms for making better new regulations have been recently set up: but not all new regulations are covered

It is important that institutions explicitly responsible for promoting regulatory quality and reform are in place, not least to ensure a consistent approach across government. In particular, institutions and processes for effective law-making are needed.

Poland has a well-developed centrally-controlled system for drafting primary and secondary legislation which must be approved by the government, organised by the Chancellery of the Prime Minister. The proposing Minister prepares a text and justification report (which must since fall 2001 contain a RIA). This is circulated to bodies at the centre of government for comment. Once the draft is agreed, and approved by the Council of Ministers, it goes to Parliament (in the case of primary legislation). The President must approve the legislation, and has an unconditional power of veto.

The central bodies involved in reviewing draft government legislation are the Government Legislation Centre (GLC), the Legislative Council, the Committee (previously committees) of the Council of Ministers, and the Committee for European Integration and its preparatory team. The Ministry of Justice (responsible for a programme to codify the law) and the Competition Authority (OCCP) also play a role.

The first two bodies look at the quality of legislation. The GLC was removed from the Chancellery in January 2000, which has given it more political and practical independence (with its own budget). Its size has recently been increased to incorporate the tasks of RIA implementation. It co-ordinates the government's legislative activity, provides legal advice to government, prepares government drafts and advises on Parliament's drafts. Since September 2001 it has been responsible for overseeing the RIA process. The Legislative Council is made up of eminent lawyers and is the senior legal advisory body to the Prime

Minister. It advises on the enactment of draft primary and secondary legislation and evaluates the condition of the law, particularly in terms of alignment with the Constitution and EU law. Evaluation reports are regularly produced and published on issues such as sectoral legislation (*e.g.* tax and agriculture). It is currently evaluating the state of the constitutional law, civilian law, labour law, media, finance and private business law. The difference between the two bodies is that the GLC focuses principally on the quality of each draft measure and the appropriateness of regulatory procedures followed. The Legislative Council concentrates on the general quality of the whole legal framework.

Since 2000, the Regulatory Quality Team, an interministerial advisory body of the Prime Minister, chaired by the Minister of Economy, has been the main driver of the efforts to improve the quality of regulation in Poland. It has been the driving force in the design and implementation of RIA. From 1997 to 2001, the Debureaucratisation Task Force played an active advocacy role for deregulation, especially with respect to draft laws that affect businesses. This crucial role has now been transferred to the Regulatory Quality Team, though no official mandate has yet been issued.

Poland's rule-making procedures are comprehensive. The Rules and Procedures of the Council of Ministers cover the draft laws and secondary regulations of Council of Ministers and of ministers. These arrangements – including the recently established RIA – cover also internal measures if they are published in the official gazettes (*i.e.* Dziennik Ustaw or Monitor Polski). However, these arrangements do not cover internal measures of the administration if they are not published in the gazettes. Even if in theory these internal measure cannot confer rights or obligations on individuals, they can have significant indirect impacts on business and society (for instance, they may establish the information requirements for permits and licences). Moreover, legislation initiated by Parliament (which accounted for nearly half of all laws enacted between 1997 and 2000), as well as amendments made by Parliament to government-introduced legislation, follows its own procedures (the Rules and Procedures of Sejm and Procedures of Senate). These procedures so far have included few quality mechanism as they mainly focus on constitutional and legal coherence.

The development of institutions for applying regulations is also important: a network of reasonably effective sectoral regulators is in place

Effective institutions responsible for the application of laws and their elaboration in lower level regulation are also needed. Such institutions need to be accountable and independent at the same time, able to resist capture by interest groups. Poland now has a large number of sectoral regulatory agencies. These have been developing since the early 1990s, and EU accession is accelerating the process, though a rationalisation of agencies and other public bodies has recently been launched.

The regulators are overseen by a parent Ministry and a parent law defines their powers. These generally consist of issuing licences and advising the government on the setting of regulated prices, with the parent Ministry retaining responsibility for overall policy. They are generally considered to have achieved significant independence, not least in budget and staffing. The Prime Minister appoints the main regulators. But they are held back by the constitutional constraint strictly controlling the delegation of rule-making procedures from ministers to any other body. As a result they cannot issue secondary regulations of a binding nature and must rely on administrative measures. Competition

law applies without exception to the regulated sectors, but the framework for the relationship between the regulators and the OCCP may need to be clarified.

Local government plays a major role in regulation and needs the same quality and consistency of approach as central government: this is not yet the case

In the past decade, devolution from the centre to local governments has been a major feature of Poland's regulatory evolution. Policies and mechanisms to co-ordinate the different levels of government are increasingly important.

Poland is a national country with a uniform and integrated legal system. Devolution of power to local government is relatively new: in the communist era power was exclusively centred in Warsaw. An important part of Poland's democratisation process was to transfer power to the local level, which today consists of 2 489 municipalities (gminas), 315 counties (powiats), 65 towns with powiat status and 16 regions (voivodships). Starting with the 1990 Law on Local Self-government, the 1990s saw the establishment of the new structures and their powers. Over half of the tasks formerly performed by the centre are now the responsibility of local government. Devolution rests on a dual system of regionally elected governments and a regional "prefect" appointed by the Prime Minister and overseen by the Ministry of the Interior. One of the key tasks of the prefect is to ensure that decisions are consistent with national law, which has primacy.

Concerns exist over the way regulations are being developed and applied at the local level. In 2000, 13 637 local government acts were published. The Ombudsman has drawn attention to the "lack of transparent legal regulations and efficient instruments of supervision of local government authorities" and that "the changes enacted in 1999 brought to light problems caused both by inconsistency of the provisions regulating the powers of different levels of local government and poor co-operation between state administration and local government bodies". Overlap between the levels is a complicating factor, which can create duplication, diffuses responsibility, reduces transparency and prevents effective controls. Excessive discretion when adjudicating in areas subject to concurrent legislation or directly developed by subnational governments (such as zoning, licensing and permits for economic activity, public contracts, public service tariffs) create unnecessary burdens and may breed corruption.

A 2001 initiative to adjust the jurisdiction of the common courts to the new regional boundaries should help. Some national institutions are vigilant in picking up inconsistencies. The OCCP for example has intervened to maintain the competitiveness of local markets in cable TV, waste collection, and funeral services. But there is some way to go to ensure minimum standards of regulatory quality at the local level.

The relationship with EU legislation is also critical: the programme for accession to the EU continues to play a key role in regulatory reform

The goal of accession to the EU has been a key driver of regulatory reform, with the need to incorporate the EU "acquis communautaire" into the Polish legal system.

The National Programme of Preparation for Membership of the European Union (NPPM), adopted in June 1998, guides the adoption of the acquis communautaire. It is updated and approved annually by the Council of Ministers. The Committee for European Integration (CEI) and its office drive the process of negotiation and transposition of laws, and co-ordinates all policy issues relating to accession. Draft laws must include an opinion

Table 6. **Areas of exclusive regulatory powers of the state and levels of local government**

Policy area	*Gminas* – communes	*Powiats* counties	*Voivodships* regions	Centre
Justice				*
Pre-school education	*			
Primary education	*			
Teacher training			*	
Higher education			*	
Operation of the public health service institutions		*		
Public health protection	*			
Specialised health services			*	
Medical emergency and ambulance			*	
Spas and health resorts			*	
Social welfare services that extend beyond *Gmina* boundaries		*		
Social assistance	*			
Old age homes			*	
Social Insurance				*
Communal housing	*			
Building supervision, registry and exchange of land		*		
Water supply (treatment)	*			
Household sewage and waste	*			
Sanitary and epidemiological supervision		*		
Communal cemeteries	*			
Land amelioration			*	
Culture	*			
Support of cultural institutions where activities extend beyond communal boundaries		*		
Cultural institutions/ preservation of cultural assets			*	
Museums, art galleries, libraries			*	
Parks, open spaces	*			
Sport (and leisure)	*			
Registry of religious worship				*
Highways				*
Modernisation and upkeep of *Voivodship* roads			*	
Road construction and maintenance		*		
Gmina roads, bridges, squares, streets, traffic management	*			
Local public transport	*			
Ports				*
Airports				*
Promotion of economic activities		*		
Counteracting unemployment		*		
Protection of consumer rights		*		
Marketplaces and halls	*			
Maintenance of county facilities and public utilities		*		
Territorial development			*	
Territorial planning,	*			
Property administration	*			
Modernisation of rural areas			*	
Municipal police	*			
Nurseries and kindergartens	*			

Note: This table does not include areas of shared responsibility.
Source: SIGMA, *Public Management Profiles of Central and Eastern European Countries: Poland*, November 1999, pp. 1-23 and updated by the Government of Poland, June 2001.

by the CEI on compliance with EU law. Parliament passed the first transposition laws in January 2000. Parliamentary procedures have been changed to fast-track these laws, with the creation of a Commission for European Law, now renamed the "parliamentary" European Commission. To speed up the process, the government has been presenting "horizontal laws" to Parliament which bundle together disparate legislation needed to adopt the acquis. The European Commission has commented that it remains to be seen how this practice will affect legal transparency.

The integration of Polish law now involves about 3 900 directives, regulations, decisions and opinions representing more than 39 000 pages of legislative text. Of the 29 chapters now opened with Poland over the course of four negotiating rounds since March 1998, 22 of the 29 has so far been provisionally set aside (as at March 2002) meaning that they do not, at this stage, require further negotiation. Negotiations continue for the remaining chapters. About 300 directives have been transposed through 200 laws.

As well as transposing the acquis, EU candidate countries must ensure that it is properly implemented and enforced. The Office of the CEI is responsible for this, and civil servants and the judiciary have been trained for the work. The European Commission makes an annual assessment of progress on transposition and enforcement. It concluded in November 2001 that Poland continues to fulfil the political accession criteria, noting that further efforts are required to speed up the implementation of the 1999 civil service law, improve the capacities of the judiciary, and fight corruption. As regards the economic accession criteria, Poland has been assessed as having a functioning market economy which should be able to cope with competitive pressure and market forces within the EU in the near term, provided it continues and completes its present reform efforts, including restructuring of state-owned enterprises, improvements to bankruptcy procedures and the

Box 4. **The European Acquis communautaire**

The Acquis communautaire comprises the entire body of legislation of the European Communities that has accumulated, and been revised, over the last 40 years. It includes:

- The founding Treaty of Rome as revised by the Maastricht and Amsterdam Treaties.
- The Regulations and Directives passed by the Council of Ministers, most of which concern the single market.
- The judgements of the European Court of Justice.

The Acquis has expanded considerably in recent years, and now includes the Common Foreign and Security Policy (CFSP) and justice and home affairs (JHA), as well as the objectives and realisation of political, economic and monetary union.

Since the Copenhagen Summit in 1993, countries wishing to join the European Union must adopt and implement the entire *Acquis* upon accession, though there is some flexibility as to timing. The European Council has ruled out any partial adoption of the *Acquis*, as it is felt that this would raise more problems than it would solve, and would result in a watering down of the *Acquis* itself.

completion of the regulatory and supervisory framework for non-banking financial institutions.

Transparency of the regulatory process is fundamental to high quality regulation: substantial progress has been made but more is needed

Transparency is the central pillar of effective regulation. It is a challenging task and involves a wide range of practices, including standardised processes for making and changing regulations, consultation with interested parties, effective communication of the law and plain language in drafting, publication and codification to make it accessible, controls on administrative discretion, and effective implementation and appeals processes.

Transparency of procedures to make new rules is established by the 1996 Law on Organisation and the Rules and Procedures of the Council of Ministers. They govern the basic processes and allocate responsibilities to the institutions involved. Recent amendments of these measures include the implementation of RIA. To ensure that these procedures achieve their goals, and avoid being transformed in a new layer of administrative red tape, quality standards need to be set and overseen.

Transparency in terms of public consultation gives stakeholders the opportunity to help shape regulation, gives regulators valuable feedback on potential costs and benefits as well as the prospects for successful compliance and enforcement, and provides a safety net against capture by particular interest groups. Consultation is systematic for some groups in Poland. For example central framework laws are put to the Socio-Economic Tripartite Committee of trade unions, employers and the Council of Ministers. Sectoral laws often require consultation with traditional representative bodies. Depending on the subject of regulations the chambers of commerce, trade unions and the church are also consulted. But this approach has the effect of excluding bodies that are not specified for consultation, and in some cases there is no obligation to consult. That said, the Council of Ministers increasingly uses public consultation, and the GLC reminds proposing Ministries of the obligation to consult. The government has organised wide public consultation on major issues such the education reform, through media and leaflets. Consulted parties are generally presented with the draft law and justification report.

Consultation was further enhanced with the Freedom of Information Law, which entered into force on 1 January 2002. The law requires all public authorities at all levels of government to allow access to all public information, including internal and external policy documents, planned legislative actions and administrative decision-making. The Law envisages publication of such documents on a Public Information Bulletin, which is however not yet in place. As such, this mechanism has the potential to become a full-fledged "notice and comment" provision similar to those that exist in OECD countries which lead in regulatory reform. Through this important law, practices which have been carried out in the environmental field since 2000 have been extended to all policy areas. Dedicated enforcement of the provisions of the law should considerably improve transparency and openness of the rule-making process.

Transparency of communication is a third pillar of effective law-making. The existence and content of laws and regulations needs to be known, and citizens provided with the information to help them comply with and make use of the law. Great efforts have been made, but more is needed. The Constitution and the 2000 Law on Publication of Normative

Laws require the publication of all legal instruments for these to be enforceable. The Journal of Law (Dziennik Ustaw) and the Polish Monitor (Monitor Polski), edited by the GLC, between them publish a wide range of laws, orders and official statements. They have been available on the Internet since January 2001. An index of laws (all laws in force plus drafts under debate) is also available on the Internet. Local laws are published in the regional gazettes. Significant efforts to improve the readability of laws have been made, with a Council of Ministers requirement to be clear, precise and use plain language.

But there is scope for improvement. Despite the Ministry of Justice codification initiative, numerous amendments hinder clarity. The need for better communication is clear from the problems implementing some recent reforms. For example the simultaneous introduction in 1999 of four fundamental social reforms (public health care, social insurance, administration and education) involved complex and unclear legislation, little time for public digestion, and a defective communication strategy. This provoked a backlash against the reforms. However the government is learning from past mistakes. Efforts are being made to address the complexity of legislation: the 2000 Law on Publication of Normative Instruments requires Parliament to publish unified legal texts.

Adoption and communication of a law sets the framework for achieving a policy objective. But *effective implementation, compliance and enforcement* are essential for actually meeting the objective. A mechanism to redress regulatory abuse is also needed as a democratic safeguard and to provide feedback on regulatory effectiveness. Poland has an array of mechanisms to ensure that the administration is accountable and that enforcement is fair. Judicial review of administrative decisions – a constitutional right – may be invoked through the courts and tribunals. The 1960 Administrative Procedure Code provides for appeals against an administrative decision to a superior body, ending with the Supreme Administrative Court. The 1991 Law on Enforcement of Administrative Proceedings (most recently amended in 1996) establishes rules and mechanisms to ensure fair enforcement and to clarify the nature of enforcement actions.

But the judicial system suffers from long delays, a major challenge, especially in Warsaw where criminal/correctional procedures take 40 months on average (against 6 elsewhere). Delays also afflict routine court decisions in commercial matters such as contract enforcement. These delays provide an incentive for bribery and corruption, and encourage Poles to avoid the judicial system and take their complaints to the Ombudsman. The government has taken some action to redress the situation, including a new judicial layer of 400 chambers, a law to simplify civil procedures, improvements to registration systems, training, and higher salaries for court employees. Critical reports (notably from the European Commission) on the extent of corruption have prompted counteracting initiatives, which include domestic laws, the ratification of relevant Council of Europe and OECD conventions, and the preparation of a Code of Ethics for civil servants. The Ombudsman, a highly respected independent Office appointed by Parliament and with a very wide jurisdiction, plays a central role in reducing corruption and increasing accountability, and produces critical annual reports on the system.

These initiatives do not meet all the needs. The judiciary needs significant strengthening – a long-term challenge – with training, public investment and improvements to the legal framework. Ex-post assessment of regulators' performance would also help. The constitutional right to appeal against administrative decisions is not

enforced by any specific mechanism: this could be helped by the recently enacted Freedom of Information Act.

Alternatives to traditional regulation need to be considered: initiatives in the environmental field are promising and should be encouraged elsewhere

The use of a wide range of mechanisms, not just traditional regulatory "command and control" instruments, for meeting policy goals needs to be kept in mind. The Ministry of Environment has taken the lead in Poland. For example it is signing covenants with major polluters on the timetable for installing new technologies to meet new standards and the ministry rewards leading companies annually with the title "Leader of Poland's Ecology". It has also developed financial mechanisms to raise money for environmental protection. But more is needed. Some promising alternative approaches such as emission trading are not yet exploited. Many decisions on the choice of regulation are driven by the needs of EU accession or special interest lobbying rather than an objective assessment of the best approach. There is a need to spread the idea of alternative approaches across government, beyond the Ministry of Environment, by incorporating it in the law-making process.

Regulatory Impact Analysis is a powerful tool for effective new regulation: implementation and enforcement of RIA need to be forcefully pursued

Poland already has a "justification report" as part of the process of drafting new laws. This report assesses the potential impact of the proposed law, covering the current situation, the changes that the law would make, the expected social, economic, legal and financial impact, financing the law, and proposals for public consultation. Several key bodies oversee the process. Since fall 2001, an RIA needs to accompany the "justification report". This is a major achievement following many months of discussions and research steered by the Regulatory Quality Team. But RIA is a long-term investment in regulatory

Box 5. **RIA best practices**

Maximise political commitment to RIA

Allocate responsibilities for RIA programme elements carefully

Train the regulators

Use a consistent but flexible analytical method

Develop and implement data collection strategies

Target RIA efforts

Integrate RIA with the policy making process and begin as early as possible

Communicate the results

Involve the public extensively

Apply RIA to existing as well as new regulations

Source: OECD (1997), *Regulatory Impact Analysis: Best Practices in OECD Countries*, Paris.

quality: its results do not come through immediately. Effective enforcement will be needed, as well as constant high level political support, to ensure effective results.

Based on OECD guidelines, RIAs will be prepared by the proposing ministries and overseen by the GLC. They will focus on implications for the public finances, including central and local budgets, the labour market, domestic and foreign competitiveness and regional development.

The following list, based on OECD experience elsewhere, sets out the most important areas for government attention in the further development of RIA:

- *Maximise political commitment to RIA*. Use of RIA should be endorsed at the highest level. All rule-making bodies should actively participate. The recent amendment to the Law on Organisation establishing RIA is an excellent base for its adequate implementation. Mandating the signature by Ministers of RIAs before the adoption of a law by the Council of Ministers would also help.
- *Allocate responsibilities for RIA carefully*. Ownership by regulators needs to be carefully balanced with quality control and consistency: responsibility for RIA should be shared between Ministries and a central quality control unit. The new initiative, which puts the GLC in overall charge, should work well, provided that non-legal expertise is available to support them.
- *Quantify impacts*. An effective RIA needs a soundly-based quantitative analysis. The newly established RIA system requires proponent ministries to "quantify costs and benefits" of draft regulations using various evaluation tools. Attention will need to be paid to three potentially difficult areas. First, the economic capacity of rule-drafters in ministries and of GLC – a legal entity – to do this needs to be developed. Second, RIAs need to distinguish clearly between the financial impact on government and that on the economy and society at large (starting with compliance costs for business). Third, RIAs should include impacts on consumers.
- *Develop and implement data collection strategies*. RIA quantitative evaluations are only as good as the data they rest on, and data issues are known to raise problems. The development of guidance for Ministries on this is essential. The availability of resources for RIA drafters is equally important.
- *Train the regulators*. Regulators need the skills to carry out high quality RIA. The government intends to publish guidelines for enhancing their skills. However training will also be essential for an administration that is more legally than economically focused.
- *Target RIA efforts*. RIA is a difficult, resource intensive and long-term process which is often vigorously opposed by Ministries with little time or resources. Experience shows that central units like the GLC can be swamped by RIAs on low impact regulations. And RIAs are often prepared at the end of the law making process: little benefit can be expected if a process that draws its strength from early roll-out is ignored until the end. Poland could set up different targeting mechanisms, ranging from setting up a clear threshold of expected impacts requiring a substantive analysis to the development of a two-stage RIA submission to GLC – the first one simply notifying the oversight body about the commitment, or not, to prepare a more evidence-based RIA.
- *Integrate RIA in the policy making process*. As part of the 'justification' report, the current system is integrated in the interministerial consultation processes. It will be important

to assess coherence among policy areas and co-ordination between ministries, as RIAs become more common.

- *Involve the public extensively*. Consultation can provide essential data and checks on the feasibility of proposals. The government's RIA policy includes arrangements for consultation of all potentially interested parities. This is a major step forward: the justification report has no provision for consultation. Integrated to requirements of the new Freedom of Information Act, RIA has the potential to be an effective method for the successful implementation of a 'notice and comment' process.

If Parliament could also take forward an adapted RIA system, given its major role in law-making, this would considerably enhance the impact of RIA on overall regulatory quality.

Existing regulations also need attention: a big modernisation effort has been made, unnecessary "red tape" has been tackled, but there is no clear policy to maintain the quality of existing laws

Most OECD countries have massive stocks of existing regulation that has not been reviewed, often reducing regulatory quality and raising administrative burdens (red tape). Responsible Ministries in Poland monitor their regulations but this is not systematic. However three initiatives over the last decade have ensured a massive renewal of Poland's stock of laws. The first has been the need to transpose EU law. The second has been the constitutional review of the sources of law launched in 1997, which aimed to determine whether an existing measure is primary legislation or should be turned into secondary legislation. This enabled the law to be restated more clearly, reduced the amount of legislation and clarified the scope for administrative discretion. In December 2001 the government announced a list of subordinate acts, which have been revoked as unconstitutional. The third initiative is the codification programme launched in 1997.

These are big initiatives and achievements. But the focus has been on legal quality, without any policy for consistent regular review of overall regulatory quality, or the use of potentially useful devices such as sunset measures.

Efforts have also been made, in the context of improving the environment for SMEs, to reduce administrative burdens for this group. The 1999 Business Activity Law (also known as the Economic Constitution) thoroughly reformed the legal framework for the functioning of enterprises. Among other things it reduced the number of activities subject to licensing, and changed some licences into permits, which only require that statutory conditions be met (so reducing administrative discretion).

Conclusion

Poland has developed rapidly towards a democratic and market-led economy. It has at the same time laid robust foundations for a modern regulatory framework. Despite weaknesses which need to be addressed, it is now in the OECD mainstream and the needs of EU accession will continue to drive it forward. It must consolidate the changes already made and pay attention to implementation. The reforms need to be firmly embedded into the governmental, social and cultural fabric of the country.

There are many key achievements. The 1996 reforms of the central administration and law-making process have set up a durable framework for further improvements. A strong and independent Ombudsman (reinforced with a constitutional mandate in 1997) has

provided a beacon for government accountability and transparency. The enactment in 2001 of the Freedom of Information Act and adoption of a formal RIA policy are important signals of government commitment to regulatory quality. The processes set up to review proposed legislation are well-conceived, with the independent Government Legislative Centre and Legislative Council giving constructive guidance to the government. The Regulatory Quality Team has become an engaged advocate of regulatory quality management. These institutions and processes should smooth the path for an effective implementation of RIA. The 1999 Business Activity Law is a good example of light regulation to support the functioning of the market economy.

Important challenges remain. The quality of human resources in the public service is a drag on the effective use of reforms already made to institutions and processes. More work is needed to develop an effective, modern and professional civil service. Effective transparency of rule-making needs to be implemented in practice. The intense work of the last decade has focused on re-inventing the legal framework, and – perhaps not surprisingly – insufficient attention has been paid to compliance, implementation and enforcement. The roll-out of an effective RIA policy will require dedicated attention.

Most of the effort and success so far is concentrated on the central executive structures of government. Parliament lags the regulatory evolution of central government in law-making. The judiciary needs overhaul to meet the demands of a modern economy. It is a fundamental link in the institutions, which drive quality regulation: a respected and effective judiciary is essential. Local government also lags the standards that are being set at the centre and this too needs increasingly urgent attention.

Recommendations

1. Continue to enhance regulatory quality: strengthen processes and criteria for making regulations

Despite the number of initiatives to improve regulatory management, the quality of regulations can be improved, by enhancing transparency and reducing excessive discretion in their application. This will also reduce costs. The Team for Legal Regulation Quality has improved the basis for rule –making by developing a RIA policy. Additional policies such as a stronger commitment to alternatives, increased focus on compliance and further improvements of quality standards (for example a stricter enforcement of the requirement that benefits of regulation must be higher than costs) are also needed.

- Develop regulatory policy by enhancing criteria, disciplines and processes for producing quality regulations, for example through quality standards**.**
- Officially mandate an independent body to advocate regulatory reform. Consider whether the Legislative Centre could play a role similar to that of the UK's Better Regulation Task Force.

2. Strengthen key central institutions to drive regulatory policy

Regulatory reform must continue to be strongly promoted, despite the significant work already carried out. There is still much to done. Regulatory oversight should remain a core function at the heart of government.

- Ensure that the responsibilities of the Government Legislative Centre are clearly defined *vis-à-vis* other central bodies. Ensure adequate resources, including for the hiring of non-lawyer specialists.
- Establish a multiyear programme for it to build up expertise in RIA.
- Establish an annual report to Parliament by the Centre on its RIA oversight work, to strengthen accountability and influence.
- Ensure that the Regulatory Quality Team, or an equivalent high-level interministerial body, continues to play an active regulatory quality advocacy role, advising the Prime Minister on a regular basis.

3. Implement Regulatory Impact Analysis for all new regulations: establish a clear and comprehensive implementation plan

RIA can systematically help to ensure the deployment of the most efficient and effective regulations. The justification report, which has so far been required for all primary and secondary legislation has not proved sufficiently rigorous. The government has recognised this and has recently established a RIA system. This is excellent. However an effective RIA process requires sustained commitment over time, specialised skills and adequate resources. The government should therefore tackle the challenge of implementing RIA with a careful plan.

- Require RIA for all substantive new draft laws and regulations, going beyond the formal definition of primary and secondary legislation.
- Target resources on proposals likely to have the largest impacts. Require a simple RIA for all measures at the early stages of decision-making. Implement a more thorough RIA for important measures at a more advanced stage.
- Adopt an explicit cost/benefit test and develop technical capabilities for RIA in the medium term (training, data collection techniques).
- Integrate RIA into the public consultation process for new laws and regulations, and establish a two-way communication with the public on the process (make RIA outcomes available to the public and feed public comment back into the process).
- Consider how RIA can be made part of the Parliamentary law making process. For example Parliament's RIAs could build on the RIAs attached to draft government laws, with an independent joint unit to manage the process.

4. Enhance consultation and communication in the rule-making process

Consultation and communication in the regulatory process are essential to transparency. The quality, relevance and effectiveness of regulation will be much improved. The keys to success are to make consultation systematic and routine, and to make it open to all major interests. Consultation in Poland has so far been systematic for some groups (and often enshrined in the law), but this approach tended to leave others out. Recent enactment of the Freedom of Information Law requiring consultation with all potentially interested parties for all new draft laws and regulations is a significant break with the past. Further efforts should now concentrate on enforcement.

- Under the umbrella of the Freedom of Information Act, ensure that all bodies and regulators organise active consultations with *all* potentially interested parties on new draft laws and regulations.

- Make sure that the potential of "notice and comment" processes for new regulation is consistently and effectively applied.
- Establish standard procedures for active public consultation *e.g. ad hoc* meetings of interested parties.

5. Ensure effective enforcement and compliance with the new openness and accountability standards set up by the Freedom of Information Law

The Constitution requires civil servants to make their decisions public but there has not been much enforcement of this requirement. Openness and accountability of the law and regulation-making process has only recently been reinforced with the new Freedom of Information Act. This will not only improve regulatory quality but also strengthen the democratic foundations of the market economy.

- Consider steps to ensure that the law is enforced, through a dedicated institution (such as the Ombudsman), and training and stronger reporting mechanisms (such as an annual public report to Parliament) are implemented.

6. Reduce administrative discretion: improve transparency and simplify forms and procedures

The transparency and predictability of regulation needs to be improved. The complexity of administrative formalities (*e.g.* obtaining licences, tax issues) needs to be reduced. This will ease the burdens on business. It will also limit the scope for discretionary decisions by officials in implementing regulations, which encourages corruption.

- Carry out a thorough review of administrative procedures and forms of licences and permits.
  - Establish an official central registry, available through the Internet, of all administrative procedures and forms, starting with business licences and permits.
  - Make other legal documents – those issued to clarify or provide further detail – publicly accessible, at a minimum.
  - Use the registry as a tool to eliminate, simplify and rationalise formalities.
  - Analyse the impact of formalities and consider whether they should be subject to RIA.

7. Clarify and develop the framework for independent regulatory agencies

The institutional framework is already complex, yet regulatory agencies are multiplying, and their respective roles, responsibilities and scope for independent action are not always clear. A key issue is their independence from private and public interests: regulatory agencies need to be independent from the political sphere as well as the sectors they regulate. Another issue is the scope of their powers. It is not clear whether the Constitution allows regulatory powers to be devolved from Ministries to regulatory agencies. Regulatory quality and the relationship with the competition authority also need attention. The recent policy proposal on Governance and Accountability in the Regulatory Process prepared by Ireland could be used as a starting point for improvement.

- Establish a policy with clear criteria for the establishment of new sectoral regulators. Issues to take into account should include: potential impact on the overall institutional

architecture, budget, availability of technical expertise, duplication and conflicts of interest with existing regulators.

- Seek to devolve necessary regulatory powers from Ministries to regulatory agencies. As a counterpoint, consider whether accountability needs to be strengthened at the same time.
  - ❖ Test in court whether powers can be devolved from Ministries to regulatory agencies.
  - ❖ If they cannot, pursue other means to secure them independent powers.
- Ensure that quality principles and tools (*e.g.* RIA, public consultation, and high level of compliance) in regulators' processes and rule making are followed.
- Clarify links between sectoral regulators and the competition authority.

8. *Improve implementation of, and compliance with, regulatory quality principles*

Implementation of regulations, and the linked issue of regulatory compliance, needs much more attention. Although Poland has a framework of mechanisms to ensure that the administration is accountable and its enforcement procedures are fair, these are not always effective. As much of the system relies on the courts, long delays in the courts undermine it. In any event the approach needs to be much broader than judicial review.

- Focus the Government Legislative Centre on monitoring the implementation, enforcement and compliance of regulations.
- Provide an annual report to Parliament on the implementation, enforcement and compliance of regulations.
- Establish a public enquiry by the Ombudsman and Supreme Chamber of Control (national audit office), or by an independent commission, to review implementation and regulatory compliance performance in respect of a dozen key regulations, and to draw lessons for future implementation and compliance.
- Continue and develop training programmes on implementation and compliance for regulators and administrators.

9. *Strengthen the regulatory quality of local government*

The quality of regulation at local government level is poor, raising the risk of harmful regulatory competition, regulatory capture by interest groups, and corruption. New structures are in place but this has not been followed through with policies to ensure that regulation at this level is of the same quality, at least, as regulation enacted at the centre of government. Given the substantial devolution of powers, this is a major weakness.

- Take measures to confirm adequate accountability and transparency of proposed local government regulations *before* these are adopted.
- Ensure that all three levels of local government (regions, counties and municipalities) apply, at a minimum, the 1995 OECD Recommendation for Improving the Quality of Government Regulation and its check list.
- Consider benchmarking regulatory frameworks (*e.g.* number and quality of business licences) to identify best- and worst- practices.
- Promote greater transparency in the making and application of regulations.

- Promote clear division of responsibilities between different levels of local government, and systematically assess consistency of regulations between the levels.

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PART II

Chapter 3

COMPETITION POLICY*

* For more information see: "Background report on Competition Policy in Regulatory Reform" at *www.oecd.org/regreform/backgroundreports*

Background

Competition policy has been used to build up the market economy and create the conditions for sustainable economic and social development

Poland retained many of the institutions and capacities of a market economy under communism. Significant private activity continued while competition laws lay dormant. Some steps, including the 1981 Enterprise Act, and the 1988 Law on Economic Activity, were taken to promote decentralised decision-making by enterprises and free up the private sector. The economic "shock therapy" introduced by the government in 1989 took this a big step further, with price deregulation and changes in the legal framework for economic activity in areas such as property rights, banking and, not least, competition law.

Poland was the first central European country to enact a competition law and establish an enforcement agency after the changes of 1989. The 1990 law generally followed standard European competition concepts, but included features that were designed to address the need to transform the economic structure and establish competitive market conditions. It set up the independent Antimonopoly Office (AMO), with a President appointed by the Prime Minister, to implement it. Though not a member of the Council of Ministers, the President took part in government work on economic issues. The AMO's decisions could be appealed to the independent Antimonopoly Court. It was transformed into the Office of Competition and Consumer Protection (OCCP) when it was given consumer protection responsibilities in October 1996. Further changes to the law were made through the 1990s, in particular broader coverage and higher thresholds for merger review.

The latest competition law development is the 2000 Competition Act introduced with the objective of fully incorporating the competition policy "acquis" of the EU into Polish law. Preparing this law has been a major activity of the OCCP over the last few years. It aligned Poland's rules with the EU's provisions on restrictive agreements, further increased merger reporting thresholds, and substantially strengthened the OCCP's rules and procedures for enforcement. The new law became effective in April 2001: so it is still early days for making a full assessment of its effectiveness.

The overall strategic objective of Poland's competition policy is to create the conditions for sustainable social and economic development and to meet consumers' economic aspirations. The economic objective is efficiency, which includes making businesses more responsive to market signals, improving their competitiveness (through lower costs), eliminating monopolies in sectors that had not faced competition, rationalising production and distribution costs, and improving product quality. The social objective targets the needs of consumers, including protection of their rights, reinforcement of their bargaining power, and the expansion of choice. The two objectives can be expected to mutually reinforce each other: competitive pressure promotes consumer protection.

Conceiving the purpose of competition policy as creating the market conditions for sustainable development emphasises its origins and continued role in the transition process. Since the early 1990s efforts were harnessed to the high priority task of developing competitive markets through the structural agenda of demonopolisation, privatisation, and import liberalisation. Profound pro-competitive structural reforms were made in the 1990s.

The Constitution contains strong statements of support for competitive markets. It states that the nation's economic system is based on a market economy, freedom of economic activity, and private ownership, and that restrictions on freedom of economic activity can be imposed only by law and only when justified by an important public interest. This provision seems to imply a presumption in favour of competition, putting a burden on the government to justify anti-competitive measures. But it is not clear that the burden is very heavy.

The AMO was active in the first stage privatisations (it issued 1 500 opinions between 1991 and 1995). Its interactions with the privatisation agency were not made public. It claimed that its opinions were usually heeded, though its views did not always prevail (for example its recommendation that the gas industry be split up has still not been given full effect, and an auto production deal went through despite its concerns).

The OCCP's participation in privatisation decisions remains informal and internal. It is not clear how well it is integrated in this process *before* bids are presented. Early involvement could forestall the possibility of competition problems clashing with revenue raising objectives if, for example, acquisition by the highest bidder would increase concentration unacceptably. Having the OCCP fully involved in the design of the privatisation plans would avoid this risk.

A 1998 government programme prepared by the OCCP, "Counteracting Monopolies and Strengthening Competition", set out the action already taken to promote competitive markets, and what still needs to be done. Specific tasks and responsibilities were allocated to Ministries, which reported regularly on progress to achieve them.

Competition policy has now moved into a new phase: as well as the continuing network sector liberalisation agenda, there is a new focus on state aids, and the need to ensure that competition policy rules are effectively applied

Most of the tasks in the 1998 programme have been completed, though some important ones need ongoing attention, especially in the traditional network sectors. The liberalisation of the postal, gas, electricity and telecoms sectors is slow and far from complete, even allowing for the difficulties of promoting competition in these sectors. Two big further challenges need to be tackled. The first is the need to apply the new rules to control state aids, which can distort competition. The most recent accession report acknowledges progress, noting that the OCCP's new department of state aids has issued nearly thirty opinions by September 2001, four of them negative.

Another challenge will be to achieve the transition in competition policy priorities, as Poland completes the transformation of its economic system, from ensuring conditions for competitive markets to ensuring that market players are obeying the rules that govern those markets. The 2000 Act has increased the OCCP's investigative powers and created some new procedures. Meanwhile, the Antimonopoly Court has become increasingly active, while some aspects of its jurisdiction and role will need to be clarified by experience

and perhaps by further court rulings. Enforcement of competition law is shifting from a process of application and administrative decision towards a model of investigation and prosecution in court.

The central institution for competition policy must balance its roles, remaining independent of government in making decisions, while staying close enough to policy-making to have an influence

The OCCP is a separate institution, not within a Ministry, and its legal powers reside formally with its President, who is not a Minister but can take part in government policy debates. Its powers are to ensure compliance with the laws on competition and consumer protection, to monitor the effect of state aid on competition, to oversee the protection of

Box 6. **Structural reforms to create market conditions**

Poland made profound pro-competitive structural reforms in the 1990s (OCCP, 2001):

- Removal of legal restrictions on undertaking economic activity;
- Elimination of state commercial monopolies;
- Introduction of competition in trade and services;
- Abolition of the state monopoly on domestic trade in products such as alcohol, fuel, coal, steel, and pharmaceuticals;
- Abolition of state monopolies in banking, insurance, radio, and television;
- De-monopolisation of economic sectors not previously subject to competition, such as agricultural machinery, coal, steel products, construction materials, seeds, agricultural commodities and processing, trucking, bus transport, and timber;
- Abolition of the state monopoly in foreign trade, leading to development of distribution networks for foreign firms and stronger intra- and inter-brand competition;
- Removal of legal barriers to the development of competition in sectors that were previously exempted by law, such as energy, railways, media, telecommunications, and postal services;
- Privatisation of many sectors and businesses, with the participation of both Polish and foreign investors;
- Development of banking and financial services, with currency exchangeability and relatively stable exchange rate;
- Allowing foreign firms to transfer or re-invest profits and abolishing many administrative permit requirements for doing business;
- Adoption of policies to encourage small and medium sized enterprises; and
- Introduction of modern statutes about competition, consumer protection, unfair competition, and intellectual property.

consumer rights, to develop or comment on draft regulations on competition and consumer rights, to prepare the government's policies on the latter, and to liaise with international counterparts. It is based in Warsaw, with nine regional offices.

The OCCP does not have formal independent status, but has demonstrated considerable independence in practice, taking enforcement actions which have sometimes been contrary to politically prominent interests. The 2000 Act has provisions to secure it more formal independence. The OCCP President will continue to be appointed by, and report to, the Prime Minister, with nominees selected through a contest, while tenure is protected by a five year term of office and the Act specifies only a few permitted reasons for dismissal.

The direct reporting relationship to the Prime Minister has helped the OCCP to participate directly in the government's major structural and sectoral reform programmes. The President takes part in the legislative process and attends meetings of the Council of Ministers on competition-related issues. This is an important role which needs to be carefully balanced with independence from government.

Greater attention to public information and consultation could make the OCCP more effective. It publishes its formal decisions, but so far makes little use of guidelines. The 2000 Act requires it to publish a regular official journal with its own decisions as well

Box 7. **Most recent "transition" steps: the 1998 program**

The scope of actions taken, and of those still needed, is set out in the 1998 government program, *Counteracting Monopolies and Strengthening Competition*, which was prepared by OCCP. This program defined specific tasks and assigned responsibilities for fulfilling them to ministries, which reported quarterly on their progress in achieving those goals (OCCP, 2001). When that program appeared, the principal successes appeared to be in wholesale and retail trade, catering and tourism, housing renovation and construction, asset management, leasing, publishing, information technology services, and the food, clothing, furniture, household equipment, computer hardware, printing, and automotive industries. Two typically thorny areas, broadcasting and agricultural co-operatives, had been de-monopolised. And decisions implementing the competition law introduced competition for municipal services such as waste disposal and funeral services (OCCP, 2001).

The 1998 program also identified some sectors where, despite the end of state-owned monopoly and the introduction of some market mechanisms, competition was still incomplete. These included coal, rail, buses, and sugar. The program concentrated its action plans on traditionally monopolised sectors that might become competitive through technological or regulatory change: electric power, gas, telecoms, rail freight, postal services, and petroleum (OCCP, 2001). Most of the tasks in the 1998 program were implemented by 2000 (although several are, realistically, described as continuing indefinitely). The last quarterly report in 2000 focused on actions needed in telecoms, electric power, hard coal, transport, and postal services. One immediate result was a government decision eliminating fuel transport permits.

as those of the Antimonopoly Court and others, and information about activities. The Act requires secondary legislation to give effect to key provisions such as block exemptions, and a process to exchange views on this with the public and business could improve the quality of the rules.

The OCCP has increased its staff significantly over the last few years. Staff levels increased by over 17% between 1996 and 2000 as sections were added for consumer protection and state aids. It faces the common problem of attracting and retaining junior staff in competition with other regulators and the private sector. Resources for purposes other than central staffing are constrained. It is difficult for the OCCP to hire experts or to conduct or buy market research. There is no extra budget for the publication of the official journal mandated by the 2000 Act.

The OCCP puts most of its effort into the problems of large firms. The overwhelming majority of its cases are about abuse of dominance and mergers. Few resources are devoted to restrictive agreements (the OCCP believes there are relatively few of these). In 1999 more than half of the OCCP's findings of violation concerned firms in municipal services, 15% in energy, 11% in water and sewer services, leaving 25% for the rest. The number of cases signalled to the President of the OCCP is increasing rapidly.

Competition policy advocacy works mainly through internal government consultation rather than public debate. A public advocacy voice by the OCCP would be welcome. Internal advocacy has been very strong from the outset: a major task of the AMO was commenting on competition-related legislation (more than 500 "standpoints" were generated between 1990 and 1995), and the OCCP continues the tradition. The OCCP also sits on *ad hoc* task forces to review policy issues, including bodies working on sectoral restructuring and reform (for example the OCCP President chaired an energy task force set up by the Council of Ministers which produced plans for electricity sector privatisation and rules of operation). The OCCP's advisory role in restructuring and privatisation is generally effective.

This "within the system" advocacy seems well adapted to Poland but raises the danger of drawing the OCCP too far into "ownership" and thus acceptance of a compromise competitive outcome. Some evidence of this tendency is the OCCP's support for antidumping complaints and some other controls on imports that other competition authorities would often oppose.

Poland now has a sound and complete substantive competition law which follows that of the EU: it needs to be vigorously applied

Poland's general competition law has been updated with the 2000 Act. Its short and familiar substantive rules are modelled on those of the EU. Investigative and enforcement powers and procedures are unusually strong. The 2000 Act is centred on a concise definition of 'relevant market" which includes product and geographic aspects, as well as sensitivity to actual consumer behaviour and to quality.

Restrictive agreements

The 2000 Act prohibits agreements that have the objective or effect of eliminating or restricting competition in a relevant market. As in nearly all OECD countries, little distinction is made between horizontal agreements among competitors who occupy the

Box 8. **Competition advocacy for regulatory reform**

From the outset, commenting on competition-related aspects of legislation has been a major task. The AMO's legal department generated more than 500 such "standpoints" on draft legislation from 1990 to 1995 (Fingleton, 1996, p. 93). That activity continues unabated. In 1999, the OCCP commented on legislative proposals about Special Economic Zones, regional development, air transport, postal services, civil procedure, large retail complexes, toll roads, environmental protection, public administration, tenant protection and municipal and public housing, prices, and the sugar market. It provided opinions about government programs concerning chemical production, SME policy, energy policy, telecoms development in rural areas, transport policy, land use planning, railway restructuring, coke industry restructuring, coal mining adjustment and restructuring, and trade policy (quotas and tariffs). It submitted comments to the Minister of Economy about coal mining reforms and to the Treasury minister about privatising and restructuring the oil industry, and about other privatisation issues, as well as trans-border TV broadcasting, the annual intervention program of the Agricultural Market Agency, and a draft document on "General assumptions for the program of emerging and developing producer groups in Poland" (OECD CLP, 2000, p. 4).

All government proposals must be consulted among all departments, including the OCCP. The time available for a response can range from one hour to three weeks. The OCCP ignores those that are obviously outside its area of concern and sends the drafts it does care about to its legal and relevant substantive departments for review. Despite the absence of formal public comment procedures, producer interests often learn about what is being considered and approach the OCCP about its views.

One common avenue for influencing policy is participation in continuing or *ad hoc* task forces. OCCP representatives served on a team for the "elimination of red tape in the economy," which developed the new law on economic activity. This law significantly reduced the number of services for which a licence would be required, and thus expanded the scope of services for which entry would be permitted subject only to an authorisation made generally available to anyone who met transparent "classification and technical" requirements (OECD CLP, 1999, pp. 4, 9). An OCCP representative has been a member of the Securities and Stock Exchange Commission, and OCCP representatives are at working party meetings considering draft prospectuses.[1] Other bodies on which OCCP representatives have served or participated include the inter-ministerial commission for changes in tariffs and trade regulations (under the Minister of Economy), the council for transfer prices in electric power (an advisory body to the minister of Economy), a team for co-ordinating privatisation in that sector (under the Treasury), and a council concerned with regulatory standards and fees in water and sewer services (appointed by the chair of the Housing and Town Development Office).

1. Under Art. 147 of the law on securities trading, the OCCP analyses competition implications of share listings (OECD, 1999, p. 9).

Source: OECD, 1999.

same position in the market, and vertical agreements among enterprises in supplier-customer relationships, the exception being the *de minimis* exemption. Horizontal agreements are permitted among firms with a collective market share below 5%, and a more tolerant 10% share is applied to vertical agreements in recognition of the fact that they may promote efficiency.

Block exemptions may be authorised by the Council of Ministers, in line with EU standards. A series of block exemptions has been adopted, paralleling the latest development in the EU's legislation.

The prohibition against restrictive agreements may be broadly applied and interpreted. For example the Antimonopoly Court has found that an agreement can be demonstrated by circumstantial evidence, such as parallel activity that has no better explanation than prior understanding. However relatively few OCCP actions have targeted horizontal agreements, though there were early exemplary decisions such as the order against a cartel of 18 sugar producers with identical prices, and against 14 insurance companies (accounting for 80% of the market) setting the same commissions. Actions taken by an association that impair competition may be treated as prohibited agreements. The OCCP for example rejected an agreement by a Regional Chamber of Pharmacies limiting entry to the market. Most decisions about vertical agreements appear to have involved enterprises in dominant positions or with significant market power. A recent decision imposed a substantial fine on the dominant petroleum producer PKN Orlen for abusing its dominance via a vertical "price squeeze" between the price it charged for a raw material, ethylene glycol, and its price for the end product, anti-freeze. Several decisions have involved local or municipal services including cable TV, waste collection, and funeral services, demonstrating the importance of competition policy in promoting competitive policies at the local government level.

Abuse of dominance

The 2000 Act characterises dominance on the EU model: a position that enables a firm to prevent efficient competition in the relevant market by creating the opportunity to operate substantially independently from competitors, contractors, and consumers. Dominance is presumed at a market share of 40%, but this is not a "safe harbour": the OCCP has found dominance at a lower share (the beer industry) and conversely it has declined to find dominance at a higher share (cable TV).

The non-exclusive listing of particular kinds of abuse includes charging prices that are too high or too low, imposing burdensome terms, restricting output, limiting technology, discrimination, tying, unjust enrichment through burdensome contract terms, onerous conditions for consumer redress, and preventing development of conditions for the emergence or development of competition (which echoes the goal of Poland's competition policy).

An abuse of dominance may not be exempted on the grounds that other policy considerations outweigh the harm to competition or customers: exemptions were eliminated by the 2000 Act. This means that it is now very important to take account of competitive realities in assessing dominance, and not to rely on formulaic market share presumptions.

The divestiture power that existed before (firms could be ordered divided or dissolved) appears to have been removed by the 2000 Act. The only remedies for abuse of dominance now appear to be a fine and an order to cease the abusive practices.

Where industries remain highly concentrated, the prohibition against abuse of dominance has been used to protect downstream customers. For example several decisions have responded to claims of abuse in the supply of petroleum products. In the network sectors most cases have foreshadowed or supplemented structural reform, by targeting abuses by network infrastructure monopolies. For example the traditional telecoms monopoly (TPSA) has been subject to several orders and sometimes fines for, *inter alia*, unjustified charges on customers and cross -subsidised tariffs.

Mergers

Large acquisitions and mergers must be approved by the OCCP in advance. The basic test appears to be whether the transaction will create or strengthen a dominant position, linked to a more general "competitive effects" test of whether it will significantly restrict competition. The relevant market is narrowly defined in terms of product, geography and time, and the degree of likely concentration is assessed, to some extent by simulation. The OCCP may impose conditions, including divestiture of assets being acquired, abandonment of control over others (including divestiture), or compulsory licensing. Approval of a merger lapses after three years if it has not taken place.

Industrial or other policy considerations may be invoked in the OCCP's merger decisions. A problematic concentration may be authorised if it contributes to economic development or technical progress or has other favourable impacts on the economy such as the improvement of product quality or distribution. This broad discretion is new in the 2000 Act. Most mergers in Poland involve privatisations or the introduction of foreign investment and management (most notified transactions are acquisitions by foreign firms), and are likely to improve efficiency. This probably explains why the OCCP has approved virtually all of the mergers it has examined.

The merger law also applies to combinations short of full acquisitions: those leading to indirect control, establishing a new joint enterprise, acquiring 25% or more of an entity's voting shares and holding management or director positions at competing enterprises. The reason for this wide coverage is not clear: it may be used more as a source of information on investments and market conditions, rather than a direct tool to promote competition.

Notification rules raise an important issue. Notification is required if the firms' combined annual turnover exceeds EUR 50 million. But market share also determines whether firms must notify. It is not required if the combined market share is below 20% – half the level at which dominance is presumed. The rule appears to be intended to reduce the compliance and enforcement burden, and because firms that should notify would have to dilute their market share by a factor of two to avoid scrutiny, the OCCP believes that important transactions would still be caught. This may be too sanguine: in other jurisdictions firms have been known to define markets creatively to avoid scrutiny.

The merger review process is straightforward. Notification is required within seven days of reaching the merger agreement. A decision by the OCCP is required within two months. The OCCP can order parties in a conditional decision to take structural measures if they proceed without notifying the OCCP, submit incorrect information, or fail to comply

with the conditions imposed by the OCCP. Information on merger filing is published in the Official Journal of the OCCP.

Some sectoral regulators also have responsibilities to review proposed mergers, although the grounds for regulatory action do not explicitly include competition issues. In banking, insurance, and investment and pension funds, merging firms must obtain prior regulatory consent.

Restructuring mandated by law is exempt from the notification and approval requirements. An example is the 1994 law mandating consolidation of the sugar industry.

Nearly all mergers have been approved without conditions. Most merger enforcement is directed at the notification requirements rather than the competitive merits of the transactions. In 2000, the OCCP issued 1 060 permits for mergers, and imposed 52 fines for non-compliance with notification. Some concerns have been expressed about the OCCP's decision making standards, given the small number of decisions, and lack of detail in statements approving mergers.

State aids

Poland's new law on state aids, which generally adopts the concepts and rules of the EU, became effective in January 2001. In principle, the law prohibits aid that may significantly distort competition or substantially hinder the development of competition, unless the anti-competitive effect is limited in time and the aid is part of a regional policy or restructuring programme. In practice, the law relies (as does EU law) on technical rules more than a direct assessment of actual effects in particular market circumstances. The law is administered by the OCCP which has a state aid unit. Experience applying the law is still limited.

Competition in public procurement is administered by the Public Procurement Office. The law on public contracts applies where the estimated value is over EUR 3 000, but simplified procedures may be applied if the value is under EUR 30 000. The law was amended in June 2001 to bring the procurement rules into conformity with EU standards (eliminating national preferences and providing non-discriminatory market access) by the end of the accession transition period (January 2004).

Unfair competition

Poland's law about unfair competition is based on the same constitutional guarantees of economic freedom that support the 2000 Act. Its general clause defines "unfair competition" as action by an entrepreneur that is "reprehensible" because it threatens or violates the interest of another entrepreneur or a customer. Typical problems are deception and mislabelling about origin, misuse of trade secrets, inducement of breach of contract, passing off, and disparagement (and unfair praise). The rules about unfair competition are enforced by private civil suits, brought by one business against another. Penal sanctions are available in theory, but rarely used. Some consistency between the private law of unfair competition and public competition concerns is ensured by giving public bodies, including local consumer advocates, business and consumer organisations, and the President of the OCCP, the right to appear in these private cases concerning violation of law or collective consumer interests. The OCCP can also bring court actions under the unfair competition law.

Poland does not have a law prohibiting so-called "abuse of economic independence": that is to say, the exercise of unequal bargaining power by a firm that does not hold a dominant position in a relevant market. The typical example is a complaint about how large integrated retailers deal with suppliers. But some issues, such as "aggressive pricing", are more likely to benefit consumers than impair competition, especially if the firm does not have market power. The government is considering putting a prohibition into the framework of unfair competition law. This will need to be handled with care to avoid impairing competition.

Consumer protection

Consumer policy is integrated into competition policy by giving both responsibilities to the OCCP. The OCCP's consumer protection powers include educating businesses and consumers about consumer rights, dealing with other state administrative bodies on the issue, overseeing product safety, co-operating with local governments and international organisations, supervising product testing by consumer organisations, and publications and educational programmes. The Trade Inspectorate reports to the OCCP President. Some of the pressure of being the "hotline" for complaints has been relieved by the recent establishment of consumer Ombudsmen appointed and funded by local governments.

Consultation with consumer interests about regulation and reform is limited, largely because of resource constraints on those organisations. The 2000 Act for the first time regularises the consumer organisations' status, provides for some funding, and requires consultation with them.

Enforcement powers have been substantially strengthened: and the focus for action in some cases is entrusted to the courts

The 2000 Act substantially modified the competition law enforcement process. Before, OCCP proceedings generally followed the Code of Administrative Procedure, with some modifications in respect of evidence based on the Code of Civil Procedure. The new rules, specifically designed for competition cases, are intended both to simplify proceedings and to facilitate investigations. Decisions of the President of the OCCP can be appealed to the Antimonopoly Court and for that reason the Antimonopoly Court often gives the final ruling (which can be changed only by the Supreme Court) in the most important cases.

Complaint procedures

Complaints may be filed by firms or associations with an interest, local governments, state inspectorates, or consumer advocates or organisations. The OCCP can also initiate proceedings *ex officio*. A fee of PLN 1 000 is normally required for bringing a complaint, which can be waived if the case is of importance to competition policy or consumer interest or if the complainant is natural person. An "explanatory" investigation may be started by the OCCP President, to assess the possibility of violation of law and the market conditions, particularly to determine whether there is a dominant position. This is also used to screen complaints. A formal "antimonopoly investigation" may follow and lead to fines. Decisions are taken on the basis of administrative and civil procedures, and proceedings based mainly on documents. Hearings may also take place.

Parties may reach a negotiated settlement, as long as that is not in conflict with the public interest. Consent-order settlement is possible in minor cases: the OCCP President

finds that the violation is obvious, the respondent may agree, and the case may be terminated with an order to cease and desist. In such a case no fine is imposed.

Investigation powers

Powers of investigation are now extensive, following the 2000 Act. In a formal investigation, parties are obliged to provide the information requested. The OCCP may summon witnesses for oral testimony, and may call on expert witnesses. Hearings are public, unless confidential information is being examined. Inspectors (from the staff of the OCCP or the Trade Inspectorate) are empowered to enter premises, inspect files and records and make copies and extracts, and request individuals to provide explanations. Further searches are possible with Antimonopoly Court authorisation obtained through the OCCP President. The inspector may also take physical custody of evidence.

Deadlines

Full antimonopoly proceedings concerning restrictive practices must be completed within four months, though the deadline can be extended under the provisions of administrative law. Merger proceedings must be completed within two months (14 days for tender offers and open-market purchases and for bank mergers).

Sanctions

The basic enforcement sanction is an order to cease and desist, backed up by fines for non-compliance. If the OCCP President finds that the law has not been violated, a decision to that effect is issued. The President can also apply the exemption conditions in individual cases to permit restrictive agreements that would otherwise be prohibited. Price control powers were not included in the 2000 Act. But in some cases an OCCP order may have the same effect. A new remedy provision is based on market share: if the parties demonstrate a "permanent decrease of their market share" below the level that would support the finding of a violation, the President would find a violation but not impose any order. This could deter vigorous competition if firms seek to keep their market share below the relatively low thresholds.

In merger cases divestiture or other corrective remedies may be ordered if the parties submit incomplete or misleading information, fail to comply with the conditions imposed by the OCCP, or flout their notification obligations. So far, these remedies have been rarely used.

Fines may be imposed by the OCCP for substantive violations, ranging up to EUR 5 million (but not over 10% of a firm's annual income). To enforce compliance with investigative process and notification requirements, the OCCP may impose fines of from EUR 200 to EUR 5 000, even for unintentional violations. Violation of the merger reporting rules will result in a fine from EUR 1 000 to EUR 50 000. Continued failure to comply with an order can incur cumulating fines at a rate of from EUR 10 to EUR 1 000 per day. Compliance with orders is also enforced by financial penalties against individuals. Managers and members of the managing body of a firm or association that fails to comply with an order, decision, or judgement may be fined up to 10 times the average salary. These individual penalties may also apply to refusal to provide information.

Judicial review

Appeals of OCCP decisions are taken to the Antimonopoly Court, through the OCCP President, who can modify his original decision in response; the modified decision may also be appealed. The Court can reach its own *de novo* decision. A further appeal is possible to the Supreme Court, to review claims of error of law or procedural defect by the Antimonopoly Court.

The Antimonopoly Court

This specialist Court has played an increasingly important role in enforcement, as well as becoming a force in the development of policy. It often relies on principles and ideas from EU competition decisions. The judges are civil law experts with ten or more years' experience. There are now three judges, to cope with the growing caseload. The latter has grown partly because the Court's jurisdiction was expanded to include sectoral regulators. This has the advantage that policies should be applied consistently in competition cases and sectoral regulation. A significant proportion of the OCCP's decisions are now appealed to the Court, which often changes or reverses a decision. In 1999 about half the OCCP's decisions were appealed, and the Court disagreed with about half of these.

The appeal from OCCP decisions is evolving into a procedure that looks increasingly like a first instance trial in the Court. Because OCCP decisions do not become effective until the end of the judicial process, and that process may involve new evidence at the Court, the practical result may be that the Court's decision is the one that really matters. The President of the OCCP can issue a decision with immediate effect, where it is necessary for the protection of competition or important consumer interests.

The increasing number and complexity of cases is leading to delays. In 1990, its first year, the Court decided 12 cases, but by 2000 the number was 232. In the early days cases took about 3-4 months, but they now take up to a year. A further appeal to the Supreme Court can take another two years. To reduce delays it will be necessary to add more judges to the Antimonopoly Court and perhaps to make greater use of more streamlined proceedings, when the rules permit. It may be necessary to clarify some ambiguities and inconsistencies about the scope of the Antimonopoly Court's powers to review decisions by different regulators, and its authority to reach a new decision or remand for further proceedings.

Competition policy in the international context has an uneven record

Poland appears to assert extraterritorial jurisdiction over conduct abroad that has anti-competitive effects in Poland, but like most other countries it is not concerned about conduct in its own country that has anti-competitive effects elsewhere. It has found it difficult to address an international market division problem that also affects its neighbours. Bidders in the privatisation process are declining to compete in different countries in the region, with lower bids as a result. Foreign firms have the same rights and obligations as domestic firms in proceedings at the OCCP. The OCCP has entered bilateral agreements with competition authorities in France, Russia, Lithuania and Ukraine, which generally provide for mutual consultation and advice. Its ability to co-operate with other competition agencies may be limited by its statutory obligation to protect the confidentiality of evidence.

The competition law has virtually universal application: some overlap exists with the sectoral regulators

The 2000 Act establishes virtually no exemptions. Nonetheless restrictions on competition that would be inconsistent with the Act's requirements may be authorised. The Act states that it does not apply to restrictions on competition that are "exempted by virtue of separate legal acts", though it is unclear whether these must explicitly state that restrictions are exempted (the only explicit exemption is the state monopoly on running a lottery), or an exemption would apply *de facto* if conduct is authorised that the competition act would otherwise prohibit.

General competition law applies to undertakings of all kinds, whatever the form of ownership. The network monopolies (telecoms, oil and gas, rail, electricity and postal services), in which the government has substantial ownership interests, have been a principal enforcement target. It also applies to actions by local governments and again, the OCCP has been active striking down anti-competitive practices in water and other local services. There is no special treatment of SMEs though in practice the OCCP appears to pay most attention to large companies.

The law also applies to sectoral activities including sectors subject to the oversight of a separate regulatory body. There are few formal rules governing the relationship between the OCCP and these regulators. Informal relationships prevail, and as most of the regulators are quite new (except for electricity) there is little experience of co-ordination. The OCCP is involved in the restructuring issues that are still a major feature of some of these sectors, as well as taking up specific anti-competitive practices.

In the electricity sector, there is some overlap of powers, for example in addressing complaints over power transmission access. Effective co-operation mechanisms appear to be in place for this. The OCCP devoted considerable attention to telecommunications before the establishment of the regulator in 2001 (including the imposition of the largest single fine of PLN 54 million on a case concerning tariff structures). The telecoms law is more explicit than the energy law in specifying where co-operation is needed. The OCCP has also been active in transport, taking action against restrictive practices in bus services and petroleum products. A major challenge is the coal industry, part of the 1998 programme of action, which is the recipient of significant state aid and needs restructuring.

Conclusion

Poland has successfully implemented a major programme to set the foundations for a competitive market economy. Much of the necessary structural change (with some important exceptions) has been completed, a project that was clearly defined and enjoyed consensus support. It now has a sound and complete competition law, built on the EU framework, which provides strong powers of enforcement. It has an established competition authority and a strong independent specialist competition court. The legal framework should be more than adequate to deal with anti-competitive behaviour. A small number of issues need attention, such as the market share test for notification. And the 2000 law must be fully implemented by completing the necessary legislation.

There are important challenges to be addressed now. The first is to curb inefficient interference in the market economy through state aids and subsidies. The issues are new and domestic consensus supporting reform likely to be weaker. The structural changes

achieved in the 1990s must be safeguarded with a vigorous enforcement of competition policy (and remaining structural issues addressed). The law should start to be applied beyond the structural and large firm agenda that has dominated so far. The new enforcement powers need to be put to the test.

The OCCP must remain strong and motivated, involved in relevant policy debates and independent at the same time. An important complement to competition policy is competition advocacy – the promotion of competitive, market principles in policy and regulatory processes. Now that most EU accession issues directly relating to competition policy have been addressed, there is a need to sustain the momentum of support for the necessary follow-up work to consolidate the market economy.

Recommendations

1. Promote effective independence of the competition authority from political influence

The OCCP must be able to take independent decisions on cases, but at the same time play an effective part in government policy debates on issues affecting competition. The status of competition policy within the government structure, and the degree of independence from political control, are still contested. Some observers in Poland feel that the OCCP has sometimes muted its concerns about issues such as privatisation outcomes, in order to maintain its contact with the policy process.

- Enhance OCCP's status as an independent institution by applying the provisions of the 2000 Act.

2. Make state aid control a high policy priority

Addressing structural issues – that is to say, promoting market structures for effective and sustained competition – remains a high priority. State aids or subsidies are now a key threat to well-functioning markets. Devolution of powers to local government (an important potential source of subsidies) makes this even more important – and an even greater challenge – than before. The means for combating harmful state aids are technically complex and this challenge too needs to be addressed.

- Confirm and promote the OCCP's new powers to monitor and control state aids, based on the general principle that state aids which distort competition should be prohibited.
- Ensure that OCCP implements its planned technical training programme for staff to equip them for this work.

3. Provide sufficient resources for the competition authority to retain staff and perform new functions

The OCCP needs the resources to perform its functions under the 2000 Act. It also needs to be able to retain staff, especially junior staff, who may otherwise be lost just as they become effective, with competitive pay.

- Consider whether additional staff are needed to cover the OCCP's expanded role under the 2000 Act (for example state aids work, outreach including publication of the official journal).

- ❖ Ensure that pay, especially for junior staff, is comparable to that offered by key competitors (*e.g.* sectoral regulators).

4. Reduce delays in the courts

The Antimonopoly Court is now the key decision maker in important cases: many OCCP decisions are appealed. The Court now acts increasingly as a "first instance" decision-maker. But delays before the Court takes a decision are now too long.

- Consider further expansion of the Court, to reduce the time taken for a decision to an acceptable 3-4 months (as in the past).
- Consider making greater use of more streamlined proceedings, when the rules permit.
- Consider whether there is a need for broader action to reduce court delays, which have become a systemic problem not confined to the Antimonopoly Court.

5. Promote more consultation by the competition authority in developing policy

The OCCP has not engaged in much dialogue, consultation or explanation of its work and decisions (for example little use has been made of guidelines to help businesses understand how competition law is applied). More open dialogue with groups affected by its policies (especially businesses and consumers) would also benefit the OCCP, improve the quality of its guidelines and regulations, and encourage a public "advocacy" voice in competition issues on the part of affected groups.

- Make sure that the OCCP uses its authority (clarified by the 2000 Act) to issue explanations and interpretations.
- Encourage the OCCP to promote more open dialogue and consultation with groups affected by its policies.

6. Improve merger notification rules: eliminate the market share test

The 2000 Act in effect applies a market share threshold for merger notification (by exempting the notification of mergers with a market share of less than 20%). But market definition is often contested. Basing the notification rule on market share leads to confusion between the administrative rule about notification and the substantive rule applied to the merger at the end of the review process (for which the starting point is presumed dominance at a market share of 40%). Reporting burdens may not in fact be reduced, and there is a risk that important transactions will not be notified.

- Consider eliminating the market share notification exemption.

7. Ensure close and consistent co-operation between the competition authority and sectoral regulators

Although the shared authority of the OCCP and sectoral regulators in competition issues has not raised major problems so far, parties can be expected to test this when they challenge decisions about issues such as infrastructure rate regulation. Also confusion may arise because consultation practices are not harmonised. For example the telecoms regulator, but not the energy regulator, is required by statute to consult the OCCP on whether a firm has enough market power that it should be regulated.

- Consider establishing a more formal co-ordination process between the OCCP and the sectoral regulators.
  - ❖ Make consultation practices between them consistent, as far as possible.

8. Resist using the concept of "economic dependence" in a way that stifles competition

Enactment of a special prohibition, outside the competition law, against abuse of economic dependence is under consideration by the government. This is to deal with situations in which a firm has relationship-specific market power which enables it to extort unfair conditions from other firms. However poorly applied general rules to regulate economic dependence can impair efficiency and competition.

- Consider alternatives to a general prohibition, such as a market definition methodology that could identify problems and address them under the competition law, or tools to enhance the bargaining power of smaller firms.

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PART II

Chapter 4

MARKET OPENNESS*

* For more information see: "Background report on Enhancing Market Openness through Regulatory Reform" at *www.oecd.org/regreform/backgroundreports*

Background

Trade liberalisation has been a major and successful feature of Poland's transition to a market economy

A key policy contributing to the establishment of a market economy has been the liberalisation of international trade, and the welcome given to foreign investment. Poland quickly took steps to open up its economy after the fall of communism. The goal of joining the EU and becoming part of its single market was formally confirmed in 1991 with Poland's signature, alongside other central European countries, of an Association Agreement (the Europe Agreement) with the EU, which entered into force in February 1994. The trade-related part of this agreement, which entered into force in 1992, provided for the gradual establishment of free trade in industrial products between Poland and the EU, and reciprocal concessions in agriculture. Tariffs and quantitative restrictions on imports of most industrial goods were eliminated by January 1995 on the EU side and by January 1999 on the Polish side.

The needs of accession to the EU have driven much of the reform agenda so far. The incorporation of EU rules into the Polish legal system has affected many areas related to trade and investment, such as product regulation, taxation, competition policy and government procurement. The accession process has also required Poland to conclude other free trade agreements with EU's preferential partners in the 1990s, notably with EFTA and CEFTA.

At the multilateral level, as well as commitments on trade in goods and services in the Uruguay Round, Poland made further commitments to open its market and reduce barriers to trade in the framework of WTO agreements on basic telecommunications, financial services and information technology in 1998. Accession to the OECD in 1996 required further liberalisation of capital movements. In short, trade policy has been geared to liberalisation.

A steady and strong growth in imports has reflected the increased openness of the domestic market and the sustained growth in capital investment that has fuelled growth in productivity. The share of imports in GDP rose sharply in the 1990s, from 25% in 1991 to around 33% in 1999. Exports have also grown, but at a slower rate than imports, and Poland has run trade deficits over the past decade. The pattern of trade has evolved significantly following the disintegration of the COMECON market, with the EU becoming Poland's main trading partner. Exports have moved up the value added ladder with manufactured goods now accounting for 80% of exports.

Foreign investment has been another key element in the transition to a market economy as it has largely contributed to the restructuring and modernisation of the economy. Over USD 30 billion of FDI was made over 1990-1999, which largely financed the current account deficits. While inflows of FDI were relatively modest in the first half of the 1990s compared to other central European countries, they gathered pace after 1995,

Table 7. **Polish foreign trade in goods**

(customs basis, USD million)

	1995	1996	1997	1998	1999
IMPORTS	29 050	37 137	42 308	47 054	45 911
Developed countries	21 595	27 326	31 107	35 270	34 017
EU	18 781	23 738	26 998	31 027	29 826
EFTA	902	939	1 045	1 051	1 145
Other	1 912	2 649	3 064	3 192	3 046
Central and Eastern Europe	4 476	5 616	6 170	6 252	6 507
CEFTA	1 625	2 161	2 652	2 974	3 071
Others	2 641	3 455	3 518	3 278	3 436
Developing countries	3 189	4 195	5 030	5 532	5 387
EXPORTS	22 895	24 440	25 751	28 229	27 407
Developed countries	17 189	17 535	17 792	20 758	20 936
EU	16 036	16 196	16 526	19 270	19 326
EFTA	359	535	395	468	561
Other	794	804	871	1 020	1 049
Central and Eastern Europe	3 885	4 911	6 043	5 971	4 652
CEFTA	1 245	1 481	1 738	2 026	2 237
Others	2 640	3 430	4 305	3 945	2 415
Developing countries	1 821	1 994	1 916	1 500	1 819

Source: Central Statistical Office, Poland.

encouraged by the liberalisation of capital movements and progress in large-scale privatisation schemes involving foreign strategic investors. In recent years Poland has become the major recipient of FDI in central/eastern Europe and FDI inflows accounted for over 4% of GDP in 1999. While most of the FDI has been directed at manufacturing, FDI in services has grown faster in recent years. The largest recipient of FDI in services has been the financial system, which is now highly internationalised with foreign investors holding over 60% of the capital of Polish commercial banks.

Table 8. **Foreign Direct Investment**

	Annual inflows of FDI								Cumulated FDI 1990-1999	
	USD billion							% of GDP	Inflows in USD billion	Per capita
	1993	1994	1995	1996	1997	1998	1999	1999		
Czech Republic	0.6	0.9	2.6	1.4	1.2	2.5	4.9	9.1	15.2	1 504
Hungary	2.3	1.1	4.5	2.0	2.1	2.0	1.9	3.9	19.6	1 940
Poland	0.6	0.5	1.1	2.7	3.0	6.3	6.5	4.2	30.6	794

Source: OECD, *International Direct Investment database and National Accounts*.

Poland's regulatory environment is now fairly well adapted to the needs of market openness: but consultation and transparency remain weak and administrative procedures burdensome

In a global economy, regulations need to be market-oriented and friendly toward trade and investment. The 1997 OECD report on regulatory reform identified six "efficient regulation principles" for building these qualities into regulations, which are reviewed below.

Non-discrimination

The application of the non-discrimination principle in regulation, through most-favoured nation treatment (all foreign firms are treated the same) and national treatment (foreign firms are treated the same as domestic firms), aims to provide equal competitive opportunities irrespective of the origin of products or services and so maximise efficient competition.

This principle has been reinforced in Polish legislation, through its accession to the WTO and in the 1997 Constitution which states that "no one can be discriminated in political, social or economic life, for whatever reason", as well as the 1999 Business Activity Law, which defines the rules for conducting economic activity. Under the latter, foreign firms with a permanent office in Poland are treated the same as domestic firms, assuming there is reciprocity. Foreign firms have equal access to appeal procedures to take up concerns over the application of regulations.

Poland moved quickly to establish a liberal regime for FDI in the early 1990s. Restrictions on foreign ownership remain in a few sectors (including broadcasting, air and maritime transport, and fishing). Although their number has decreased, special permits or licences are still needed for certain activities (such as pharmaceuticals, financial services, telecommunications services, and tourist services). They apply to domestic as well as foreign firms, except in air transport for which foreign firms need a specific permission. In common with other OECD countries, there are restrictions on entry to some professional services. Restrictions are maintained on the purchase by foreigners of real estate, now mainly applied to farming land.

A noteworthy exception to the application of the non-discrimination principle is public procurement. Although the 1994 law set a general rule of non-discrimination, it also included a national preference clause, by which the procuring party had to lower by 20% the price of tenders submitted by domestic suppliers in evaluating bids of foreign and domestic firms. That said, the 1994 law considered foreign firms established in Poland as domestic suppliers, and the Office of Public Procurement could waive these rules. The new law on public procurement adopted in June 2001 foresees the elimination of this discriminatory rule upon accession to the EU, as required by the accession process, but maintains it in the interim.

Poland's free trade agreements – not least with the EU – are preferential by definition and a departure from the non-discrimination principle in that they give more favourable treatment to the countries in the agreements than to others. However they need to be judged in terms of the practical impact on trade and competition, and their transparency. In these terms they come out well. The agreements are published, have resulted in liberalisation of trade with the other signatories, and come within the limits set by the WTO.

Transparency

Market openness requires that all market participants be fully aware of regulatory requirements so that they can base decisions to trade on an accurate assessment of costs and benefits. This is especially important for foreign firms which have to cope with differences in the business environment, such as language and business practices. Transparency requires access to information on regulations and openness of the rule-making process through public consultation.

All laws must be published in official journals and in 2001 the government started to post this information on the Internet. As a specific help to foreign firms, the Polish Agency for Foreign Investment (owned by the Treasury) acts as an intermediary between potential investors and the administration. It provides firms with information regarding investment conditions and procedures, assists in contacts with Polish authorities and business authorities, and facilitates business partnerships. The Agency is to be merged with the Polish Information Agency in the near future.

Consultation in rule-making has developed in recent years, though it needs to go further. Consultation with trading partners can also take place in the framework of the WTO, especially for technical regulations and standards as well as phytosanitary measures, which are covered by the Agreements on Technical Barriers to Trade (TBT) and on the Application of Sanitary and Phytosanitary Measures (SPS). The Polish Standardisation Committee, which is responsible for elaborating standards, notifies its annual programme of work and draft standards to the WTO TBT Committee. At the national level, draft standards are posted on the Internet and all parties, including foreign parties, may comment.

With regard to public procurement, transparency rules were set up by the public procurement law of 1994 that provide for publicising the procedures, with some limits relating to commercial secrecy. The Office of Public Procurement is responsible for the publication of tenders, the preparation of draft regulations on public procurement, approving the choice of bidding procedures, and collecting information on the performance of the system. All tenders above a certain threshold (Euros 30 000 for unlimited and two step tendering) must be published in the Public Procurement Bulletin, which is also available free of charge on the Internet. Transparency will be enhanced further with the obligation to make all tenders public on the Internet sites from October 2002. Better access to information has resulted in an increase in the average number of bids received per tender in recent years. That said, a tendency to make detailed formal requirements have excluded some bidders.

Avoidance of unnecessary trade restrictiveness

Where possible, regulators should favour measures that have the least restrictive effects on trade, a principle that is included in several WTO agreements. Mechanisms need to be put in place to give effect to this principle, including an *ex ante* assessment of the impact of proposed regulations on trade and investment, and streamlining procedures.

Poland already has a mechanism (the justification report which must be attached to all draft laws) for considering the impact of a new law. Trade and competition experts are consulted on drafts as part of the inter-ministerial consultation procedure. The current system is effective in identifying potential violations of international obligations but does not provide for a thorough impact analysis, and has not always led to the removal of

measures that restrict trade such as import constraints. The government has now committed itself to implementing a much more rigorous Regulatory Impact Assessment (RIA) based on OECD principles. This initiative should favour the development of regulations better adapted to open markets: it specifically mentions international competitiveness. With trade and investment however, the challenge is to go beyond checking legal compliance with international commitments, and to assess the practical impact on imports and exports and investment (which is not explicitly embodied in the RIA procedures). These issues must be integrated into guidelines and training for RIA. The presence of trade experts in the Government Legislative Centre, and systematic consultation with firms, would help.

Another key issue is administrative procedures. These often result in delays, uncertainties and costs for business. The government has recognised this. A codification programme for existing laws started in 1997, and the 1999 Business Activity Law has reinforced the legal environment in which businesses operate. The number of activities subject to licences has been reduced, and some licences have been replaced by permits. But there is considerable scope for improvement. Business complaints cover burdensome requirements, excessive official discretion, and the time taken to handle administrative procedures. A survey of foreign investors commissioned by the Polish Agency for Foreign Investment drew attention to legal loopholes, lack of regulatory coherence, frequent changes, and excessive detail. Building permits, real estate acquisition, work and residence permits are the most often cited. Nevertheless there was progress relative to earlier surveys.

There is a clear need to reduce administrative burdens, as well as a need to improve transparency so that firms are aware of, and understand, requirements. A central registry of procedures would be an excellent initiative.

A particular challenge exists with customs procedures. The rules have to be harmonised with those of the EU and there has been a large increase in traffic (including transit traffic) giving rise to serious border delays. The government has sought to address the problem, and a customs business strategy was adopted in October 1999, setting out the objectives of eliminating bureaucratic barriers to trade alongside adaptation to EU law, the efficient and effective collection of customs and tax duties, and supervision of trade in goods that are subject to restrictions. The strategy is monitored with the publication of an annual report. Adaptation to EU rules was mostly achieved with the adoption of a new Customs Code in January 1998. The fight against corruption – a concern raised by trading partners – is a key concern, and a code of ethics for customs officials was introduced in 2000, with related monitoring of custom officials' activities. Simplified procedures have been introduced, and their use has increased steadily. The development of a selective system of control based on risk analysis is being taken forward.

But more improvement is needed. Simplified procedures are still not being used much and computerisation is still limited. Only two border points can accept electronic declarations. Computerisation of customs offices is limited and border points not always connected, impeding information exchange.

Use of internationally harmonised measures

Compliance with different national regulations and standards can make the cost of operating in different markets significant, even prohibitive, a major issue raised by the

international business community. One way to reduce these barriers is to use international standards. This solution has been promoted by the WTO TBT agreement, which requires that countries should base their technical requirements on international standards. In Poland, the process of accession to the EU has generated a momentum for the adoption of international standards, by committing it to promote the use of European technical standards and conformity assessment procedures, to seek the conclusion of agreements on mutual recognition, and to participate in the work of European standardisation bodies. In particular, Poland must adapt to the EU New and Global Approach, in which regulation is limited to defining essential requirements, not detailed technical specifications. Under the New Approach, the development of standards is left to European standardisation bodies, and their use are not mandatory, although they provide a presumption of conformity. Adaptation to the EU system has involved radical changes in the Polish system, which had developed a large number of specific standards and certification requirements, and was assessed by exporters as burdensome and an obstacle to trade.

The 1993 Standardisation Law was the first major step in the reform of product regulation. It distinguished between voluntary and legally binding standards, and stated that standards should take account of international ones. The next major step was the adoption in 2000 of the Law on Conformity Assessment, which created the legal basis for transposing EU directives. A new standardisation law is under preparation, which aims at achieving full conformity with the EU system, including notification procedures.

The Polish Committee for Standardisation, reporting to the Prime Minister, is responsible for the development of voluntary standards and working with the international bodies, with emphasis in recent years on harmonising Polish with EU standards. As of April 2001 progress had been made: of 18 000 Polish standards, 75% were European, and 10% complied with other international standards. With 45% of European standards adopted, Poland still has work in progress adapting to EU standards, and lags other EU applicants in these developments.

There have also been changes in relation to certification. The 1993 law had introduced the declaration of conformity by suppliers for some products, a less costly conformity procedure than mandatory certification by specified bodies. However implementation has been delayed by the persistence of mandatory certification for many products and the lack of legislation on product liability until the adoption of a law in 2000. Progress has, however, been made in recent years in reducing the list of products subject to mandatory certification. As of April 2001, 10% of products were subject to certification, against 30% in 1997. In July 2001, the government also adopted a strategy for market surveillance.

These new arrangements have radical consequences for the organisation and work of the various bodies involved in product regulation and in particular difficulties remain in the implementation of the new system by certification bodies. This is still work-in-progress.

Recognition of equivalence of regulatory measures adopted by foreign countries

Where international standards are not available, trading partners can mutually agree to accept their standards as equivalent. Many national standards still exist, despite the development of international standards. At the same time producers are increasingly required to show conformity with national standards, which adds to costs when they sell in different markets. Mutual Recognition Agreements (MRAs), which can cover the

standards themselves or the procedures used to assess conformity, can help where the objectives of regulations are substantially the same.

The 1993 law on testing and certification authorised Poland's national body, the Polish Centre of Testing and Certification, to conclude agreements with foreign institutions. Several agreements have now been signed regarding test results. Poland has asked to negotiate a Protocol to the European Agreement on conformity assessment (PECA), a specific MRA designed to support the harmonisation process and facilitate trade by extending benefits of the internal market to sectors for which the applicant country has aligned its rules with EU legislation. Once in place, PECA allows EU exporters (but not non-EU exporters) to gain access to the market of the applicant country if their products are certified to the EU harmonised requirements without going through additional conformity assessment procedures, and exporters from the applicant country to gain the same advantage when selling their products in the EU market.

The institutional framework for certification and accreditation has been reinforced with the adoption of the April 2000 law on Conformity Assessment. This separated certification and accreditation activities and created an independent "Polish Accreditation Centre" which became operational in January 2001, and which is gradually establishing itself with other accreditation bodies, a crucial step to build confidence in the Polish certification system and promote mutual recognition.

Application of competition principles in an international perspective

The benefits of market access can be reduced if anti-competitive conduct is not addressed. From an international perspective, the important issues are procedures for hearing and deciding complaints over market access, and the institutions that deal with these. As well as a competition authority (the OCCP) and an independent Antimonopoly Court, Poland now has a complete competition law that conforms to the EU law, and strong enforcement procedures (yet to be fully tested). The law applies to foreign firms exporting to Poland. The focus so far has been on tackling structural and dominance issues, but the emphasis is shifting to state aids, which can significantly distort competition, not least at international level.

Sectoral trade and investment liberalisation has been steadily pursued: more is needed in sectors which have focused so far on domestic liberalisation

Telecommunications reform started relatively late, and there is still much to be done, but the 2000 Telecommunications Law promotes increased liberalisation, including the abolition of restrictions on foreign ownership of telecoms operators. TPSA's monopoly in international voice telephony remains until the end of 2002. Its privatisation has progressed and the largest shareholder is the France Telecom consortium with a 47.5% share. The telecommunications equipment sector has been opened to competition. Customs duties have been decreased and the recent introduction of self-certification should reduce obstacles to trade. Two thirds of imports originate from the EU.

The legal basis for opening the electricity market to competition has been set up, and the market is being gradually opened up. The 1997 Energy law paved the way for privatisation of power companies: all but one was sold to foreign investors. The international connections of the grid have been reoriented to Western Europe and additional interconnections established. Accession to the EU requires that the Polish

market be open to international competition, unless reciprocity is invoked, which is a danger. The main fuel input to Polish electricity is coal, and phasing out restrictions on imports as part of the sector's restructuring would reduce domestic electricity costs.

The automobile sector, one of the first to be privatised, has been one of the fastest growing in Poland: it now ranks eighth in Europe. Foreign firms have been encouraged to set up production plants in Poland, accounting for nearly a quarter of manufacturing investment. Over the past two years, the market share of imports has significantly increased from 36% of new registrations to nearly 75% in 2001. This gave rise to attempts to revitalise a temporary ban on the imports of used cars that was initially adopted in 1993. Some progress has been made on mutual recognition of conformity.

Conclusion

Bold reforms over the past decade have opened the Polish economy to international competition, reflected by a strong growth in imports and FDI (some sectors, notably agriculture, remain sheltered). The needs of accession to the EU and the signature of a number of international agreements have driven the reforms. Major progress has been done in building the six efficient regulation principles for market openness identified by the OECD into the regulatory framework. Domestic regulations generally give foreign firms equivalent competitive opportunities, with some important exceptions such as government procurement and real estate. Restrictions on foreign investment have been reduced. Competition policy has developed, to the benefit of foreign as well as domestic firms. The reform of standards and certification systems, which were considered an important burden on trade, is underway. Recent progress has been made to adopt EU standards, reduce mandatory certification requirements and use more flexible conformity assessment systems.

The procedures for adapting and improving the business environment could be more user-friendly. More could be done to give a stronger voice to market openness issues in the rule-making process. The preparation of regulations does not provide yet for a thorough analysis of their impact on trade and investment. Public consultation is underdeveloped and does not allow for meaningful interactions with the private sector. More could also be done to simplify regulations, especially administrative formalities. Improving the business environment is not just for attracting foreign investment but for the benefit of all firms.

As competition increases, Poland needs to ensure it is not tempted to intervene to protect the market. Traditional barriers to trade have been effectively brought down. Pressures may now arise for the use of domestic regulations to protect the domestic market, and the government itself may be tempted into protection for some industries or to mitigate the current account deficit. Transparency is essential to avoid capture in this way by or for specific interests.

Recommendations

1. *Improve the business environment by streamlining administrative formalities*

Despite progress, administrative formalities are still too burdensome and unpredictable, imposing unnecessary costs on business.

- Pursue efforts to review and streamline administrative formalities, and eliminate unnecessary ones.
  - Establish an official central registry of formalities, as part of the general registry

2. Promote effective enforcement of regulations

- Monitor the implementation of regulations and train the regulators

3. In implementing RIA for new laws and regulations, specifically integrate international trade and investment issues

- Ensure that RIA assessment criteria include trade and investment, and that these criteria are applied not just to regulations that directly affect trade and investment but other regulations (*e.g.* product or environmental regulations).
- Develop trade and investment assessment criteria based on the efficient regulation principles for market openness of non-discrimination, transparency, avoidance of unnecessary trade restrictions, and use of international standards.
- If an RIA identifies negative impacts of a proposed regulation on trade and investment, ensure that it seeks alternatives, and if necessary justifies the need to go ahead with regulations that will have a negative impact.

4. Widen opportunities for consultation with all stakeholders in the rule-making process

Despite progress, the public consultation process in developing new rules is still undeveloped. More business and consumer participation could help identify issues, contribute towards a more business-friendly environment, and promote a regulatory framework which is adapted to a market economy open to international competition. There is a need also for public dissemination of consultation exchanges, to reinforce the accountability of officials and limit regulatory capture (the risk that regulators will be diverted by specific interest groups). The participation of all potential stakeholders (for the benefit of the quality and relevance of regulation) has recently been enhanced with the Freedom of Information Act. Vigorous enforcement should now be secured.

- Establish a "notice and comment" process.
  - Provide an adequate timeframe for public consultations.
  - Publish the comments received, and the administration's response to the comments.

5. Pursue progress in the adoption and use of international standards and mutual recognition agreements

Further progress in the adoption of international standards is needed. Progress is also needed to adapt and simplify certification procedures to conform with EU procedures. Adjustment to international and EU standards and procedures has been relatively slow, and the retention of a national system of standards and certification has created major trade barriers. Where agreed international standards and procedures are not available**,** the trade barriers created can be reduced if trading partners agree to accept their measures as equivalent through mutual recognition agreements (MRAs). Effective implementation – through well trained officials – of the recently adopted legislation and procedures is important.

- Ensure that general progress in the adoption of international standards and mutual recognition agreements continues, using the impetus of EU accession requirements, the 2000 Act on conformity assessment, and the creation of the independent "Polish Accreditation Centre".
- Ensure that officials in the certification bodies are effectively trained for the new standards and procedures, and able to help businesses to adapt too.
- Set up a mechanism for effective market surveillance to ensure the development of manufacturers' declaration of conformity.

6. Continue to modernise customs procedures

Progress in reducing administrative burdens at the border, and improving the efficiency of duty and tax collection, needs to continue. There is some way to go. The use of simplified procedures and computerisation is still very limited. The framework of computerisation and interconnection needed to set up an electronic data interchange (EDI) system, which would allow selective controls based on risk analysis, is not yet in place. The tax code is complex. There is a continuing need – raised by trading partners – to fight against corruption.

- Increase the use of simplified procedures.
- Invest in computerisation and aim to implement an EDI system.
- Continue to promote co-operation between border officials. Continue to implement the strategy of fight against corruption through close monitoring.

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PART II

Chapter 5

POSTAL AND ENERGY SECTORS*

* For more information see: "Background report on Regulatory Reform in Postal and Energy Sectors" at *www.oecd.org/regreform/backgroundreports*

A. THE POSTAL SECTOR

Background

The liberalisation of the postal sector is very slow: there is a long way still to go

The postal sector in most OECD countries remains dominated by a state-owned vertically integrated monopoly, still largely protected by law from competition over most of the product range. Poland is no exception, but has liberalised even less than most others and less than required by EU law (with which it must comply for EU accession).

Polish Post is the state-owned operator, with 97 000 employees in 1997. The use of the postal system is relatively low, but is expected to rise. The 1990 Communications Act governs the postal service, which is defined as a universal service, an obligation on Polish Post. A 1996 ordinance by the Minister of Communication sets out the details concerning universal service definition, complaints procedures, letter size standards and so on.

Universal service is defined as the receipt, transport and delivery of letters in both domestic and foreign traffic up to 2 000 grams and postal parcels up to 20 kilos. This market is reserved exclusively for Polish Post (unlike in the EU where the reserved market is less than the universal service obligation (USO) defined similarly to the Polish one). Polish Post's revenue under the USO is around 73% of its receipts. The cost of USO is not known. Polish Post became profitable in 1998. It receives subsidies for investment: state aid controls will apply to this. It does not yet meet the delivery quality standards of the EU and investment in new technology is likely to be needed. It will be important that any future subsidies are used effectively for this purpose.

Polish Post had a complete monopoly of services before 1995. Some competition was allowed after this in courier services. At the end of 2000, 22 other firms operated courier services under licence (none, including Polish Post, is dominant), and around 60% of the parcel services market is private. Courier service liberalisation has been positive: a broader range of services, improved quality and a closer alignment of cost and prices in the non-reserved area. Polish Post is under no obligation to make its network accessible to entrants. Competitors have no right of access to post office boxes, the property of Polish Post. There is no specific mechanism to resolve access disputes, though the competition law applies to the sector and could be used if dominance is found (dominance has been found by the OCCP in relation to high prices for the use of post office boxes installed in postal premises).

The Minister of Infrastructure (previously the Ministry of Post and Telecommunication and later the Ministry of Communications were responsible of this sector) is the responsible policy making body. He oversees asset and financial management of Polish Post, which is a State Utility Enterprise within the governance framework established by the State Utility Enterprise – Polish Post Act 1997. He also appoints the Director General of Polish Post and board members (appointed for three years). Prices, which are uniform throughout the country for the standard letter service, are set by the Director General of Polish Post, subject to an as yet unused right of the Council of Ministers to set maximum prices.

A new draft law, if adopted, will promote modest liberalisation and bring Poland broadly into line with the EU

A new draft law submitted to the last Parliament had not been adopted before its term expired. The rule of discontinuation means that the law must be resubmitted to the current Parliament. To this end a new draft is being elaborated at present, in line with the EU Postal Directive requirements and following the basic assumptions of the previous draft. It brings the USO definition into line, proposes a phased opening of the market, requires accounting separation to identify the costs of each postal service and to base prices on these costs, and does not limit the range of activities of Polish Post. The regulatory functions in the two sectors will be undertaken by the President of the Office for Posts and Telecommunications Regulation (URTiP) from April 2002. An advisory body to the President of URTiP in the postal sector will be the Postal Services Council. The URTiP will take over regulatory functions relating to prices and permits, supervise the postal market, and advise the Minister on policy. The Minister will retain overall responsibility for policy and for determining postal business terms and conditions (notably universal service). The URTiP will be established on the basis of the current Office for Telecommunications Regulation (URT).

Under the proposed liberalisation, some 3-5% of Polish Post's current revenue from letter post items will become contestable. In May 2002, the Council of Ministers further accelerated the liberalisation pace and the reduction of the Polish Post market share by opening up postal services for domestic and cross-border mail of up to 350 grams from January 2003. The government has not ruled out the possibility of further liberalisation, especially if this is driven by the EU, and indeed this would be required under recently agreed changes to the EU Postal Directive. But it is also concerned that liberalisation, including market entry by foreign operators with capital and technology, could threaten Polish Post. A decline in its revenue may hamper its ability to deliver the USO. But Polish Post also needs to make service quality improvements and increase the range of its services: competition will encourage this.

Conclusion

Some resistance to reform in the postal sector has been encountered in Poland. This is not unusual, and reflects the fact that the postal sector is a core infrastructure sector of economies and a universal service that must be widely available to citizens at affordable prices. Liberalisation is a delicate matter. However the experience of countries that have liberalised the most is positive: a better range and quality of services and improved financial performance, as well as generally sustained employment levels. And the liberalisation mandated by the EU is modest. Poland should achieve at least this level of reform.

Recommendations

1. Accelerate liberalisation: adopt the new Postal Law

Further liberalisation of the postal sector – *at least* to the modest level required by EU law – is needed to improve performance. Liberalisation, which has been subject to resistance and delays, currently lags the international benchmark.

- Ensure passage of the new Postal Law at the earliest available opportunity, *without* compromising on the degree of liberalisation (*i.e.* the minimum consistent with the EU framework).

2. Ensure that Polish Post has robust accounting separation

Efforts to open the market will fail if the costs of each postal service provided by the dominant incumbent cannot be separately identified, with a clear distinction between reserved and non-reserved services. This is crucial to ensure that Polish Post cannot cross-subsidise its activities in the non-reserved sector (the sector open to competition) from activities under its universal service obligations.

- Ensure that the new accounting structures of Polish Post allow a clear distinction to be made between the cost of meeting its universal service obligations and the costs of non-reserved activities, and that these can be measured.

3. Consider a mechanism to fund the delivery of the universal service obligation if competition undermines the profitability of Polish Post

Polish Post is currently only modestly profitable, and its ability to fund its universal service obligations may be strained by lower revenues due to competition and the need to make substantial investments to improve service quality and offer a broader range of more competitive services. It is highly unlikely that competition will have this effect as it has generally boosted the performance of post offices in other countries.

- If necessary following liberalisation, take measures to ensure that universal service obligations can be met.
  - Should it be necessary, consider a direct fund-raising mechanism (through a charge on all operators) and use a tender process for allocating universal service responsibilities and compensatory subsidies to minimise the cost of universal service provision.

4. Ensure competition authority vigilance over Polish Post behaviour as the market is liberalised

As the dominant operator by far, Polish Post may abuse its market power to prevent the emergence of competition in activities which will be liberalised (essentially letters over 350g). This is all the more likely as Polish Post remains state-owned and thus under looser budget constraints than private companies, so it can engage more easily in anti-competitive cross-subsidisation.

- Ensure that the OCCP is vigilant to the possibility of anti-competitive practices by Polish Post (*e.g.* cross-subsidisation which amounts to predatory pricing) and takes action if these practices are discovered.
  - If accounting separation proves an inadequate basis for this approach, consider a structural solution on the basis of that imposed by the EU Commission on Deutsche Post as a remedy in an abuse of dominance case.

5. *Continue the process of corporatising Polish Post*

The further development and restructuring of Polish Post should be taken forward. The existing extensive network of post offices could yield additional value by extending the range of services provided at post offices.

- Continue to explore commercial opportunities, using as appropriate the strategy document prepared by Polish Post.
  - In particular, explore opportunities for Polish Post to expand to take advantage of network synergies.

B. THE ENERGY SECTOR

B.1. THE OIL SECTOR

Background

The government has substantially withdrawn from direct involvement in the oil sector, but privatisation has generated a high degree of concentration and integration between the wholesale and retail markets

The oil sector accounts for around 20% of total primary energy supply in Poland. Domestic production is very small and nearly all crude oil demand is covered by import. Imports can be expected to rise in response to Poland's economic convergence with Europe. Under central planning the sector was made up of state enterprises specialising in particular sectors differentiated according to function. There has been fundamental change since then to establish a market-based system, the main elements of which have been restructuring, corporatisation and some privatisation (some significant state ownership remains but is being phased out), import liberalisation, and a reform of taxation.

The state-owned Polish Oil Company (Nafta Polska), created in 1996, amalgamated most of the government's interests in refining and distribution with the task of completing the sector's privatisation by no later than the end of 2001, as originally set out in the programme "The Restructuring and Privatisation Programme of the Oil Sector" – but this timetable was not achieved with delays in the sale of the Gdansk refinery. Once the privatisation is complete Nafta Polska will be phased out. The Minister of the Economy has

Box 9. **Retail distribution**

There are around 6 500 service stations in Poland – this reflects a substantial development of the sector since the commencement of liberalisation when there where only around 1 300 stations.

Owner/Franchise	Percentage of stations	Approx. market share
Independents	56%	~35%
PKN Orlen	31%	~40%
Foreign Cos.	9%	~20%
Gdansk Refinery	4%	~5%

Note: "Independents" in the above table are not branded or franchise operators. Foreign operators include: BP, Shell, Statoil, Preem, Aral, Jet, Esso, Dexpol, DEA.

overall policy responsibility for the sector, while the Treasury Minister performs ownership functions.

Poland has two major (world scale) refineries able to produce refined products to EU quality standards: one at Plock with 75% of domestic capacity, and the other at Gdansk with 20%. Polish Oil Concern Orlen (created by merging Plock refinery and fuel distribution network CPN) was largely privatised by public offer (November 1999 and July 2000) (28.44% of company shares remain with the Treasury). Negotiations for a sale of part of these shares and also of the Gdansk refinery are continuing. Given the existing high level of concentration in this sector, the interests of some potential purchasers or merger options could raise additional competition concerns. Crude oil pipelines are owned and operated by the state-owned Enterprise for Oil Pipelines Exploitation, which are considered a strategic asset and will remain in state ownership. However, Naftobasis (Naftobaza) company (which manages fuel stores) is scheduled for privatisation. PKN also has facilities. Import facilities are privately owned and independent of the domestic refiners. Retail distribution has seen a substantial development (there are now some 6 500 service stations compared to 1 300 at the start of liberalisation).

Fuel prices were liberalised in 1997 although the Council of Ministers retain the reserve power to set maximum prices to "counteract unfavourable social and economic phenomena". The sector is subject to the competition law.

The sector must stay competitive: refining, distribution and retailing, and the import regime are actual or potential weak spots

The high concentration of the refining sector raises potential concerns. In fact PKN Orlen's market share of 75% is well above the 40% share above which dominance is presumed under the competition law. It is for this reason that the OCCP has recommended that Gdansk should *not* be privatised to PKN. This advice has been heeded but the sale is not yet finalised and there is a strong lobby for PKN to buy Gdansk. Great care will still need to be taken in deciding the successful bidder. The scope for action by the OCCP against any anti-competitive effects depends on the definition adopted for the market – whether national or regional (the latter definition would make it harder to take action).

The issue of market definition underlines the importance of having a liberal import regime. The more liberal this is, the more likely it is that the relevant market at the refinery level could be considered broader than Poland. The wider market would discipline domestic players: imports would increase if prices rose. The import regime is already liberal, with import quotas abolished from January 1997, and import duties reduced to zero from September 2000. This open market policy should be sustained. If low quality fuel imports became a serious problem the regulation of quality should be tightened instead of imposing import restrictions. Transport and storage also play an important part in the functioning of an effective regional market, and should be monitored for possible anti-competitive practices. Careful attention should also be paid to possible barriers "behind the border" from anti-competitive practices, given the vertical integration of major refiners with the distribution infrastructure (though the independence of storage and pipelines from the domestic producers is helpful).

The OCCP also has an important role to play in monitoring the possible exercise of vertical market power within the franchise sector of the branded distribution networks of PKN Orlen and Gdansk. The long term franchise contracts give scope to exert unfair bargaining power. This is a common issue, not specific to Poland. As franchises near the

end of their term, it could become a problem. It needs careful handling as intervention taken too far to protect franchisees could encourage the refiners to avoid franchising operations in future. The refiners also have scope to exert market power over non-branded distributors/retailers. Examples might include wholesale supply contracts that include "exclusivity clauses" or harsh termination terms. The OCCP has already taken two court actions against PKN Orlen for monopolistic practices: court appeals are pending.

Conclusion

Reform has been taken a long way but the oil sector is very concentrated relative to those of most other OECD countries. Privatisation needs to be completed with a view to maximising the future scope for a competitive market. Two important weaknesses in the sector's structure are the concentration of the refining industry and the vertical integration of the refiners with distribution/retailing. The first was inevitable as there are just two major refineries but the bundling of the major refiner with the major distribution network could have been avoided (was an unfortunate policy choice in the privatisation). The liberal import regime needs to be sustained to help maintain effective competition. The OCCP needs to monitor the industry closely.

Recommendations

1. Complete privatisation plans as soon as possible, taking care to promote a competitive market structure

Reform has already resulted in a substantial government withdrawal, and the privatisation plan needs to be completed to ensure an effective commercial market. But as the sector is highly concentrated and great care is needed to secure a competitive market structure. It is more effective to establish structures conducive to competition at the outset, than to rely on ex-post regulatory or competition remedies to competition problems.

- Complete the privatisation programme.
  - Gdansk refinery should not be privatised to PKN Orlen or to a company linked financially or by agreement with PKN Orlen.
  - Logistics (pipelines and storage) infrastructure (if it is privatised) should not be privatised either to PKN Orlen or to the purchaser of Gdansk. If this happens, implement a regulatory solution to ensure that the facilities remain available for all operators, for the use of independent imports and for the domestic supply of refined products.

2. Maintain a liberal import regime to promote competitive product supply

An open import regime is an important way of ensuring effective competition in refining, given the concentration of the domestic refining sector. It makes it more likely that the market at the refinery or wholesale level can be defined in regional rather than national terms.

- Sustain the current liberal import regime. Quotas or special licences should not be reintroduced for protective purposes.

- ❖ If the problem of low quality refined product imports becomes sufficiently serious and quality controls have to be tightened, avoid blanket import restrictions and adopt measures directed specifically at quality issues.

3. Ensure competition authority vigilance over the refining market

The high degree of concentration in refining and the vertical links between refining and distribution/retailing could well generate competition issues. Following privatisation, future company alliances could raise problems (*e.g.* co-operative regional arrangements between MOL (Hungary) and/or OMV (Austria) who are bidders for Gdansk, and PKN Orlen).

- Ensure that the OCCP monitors developments in company alliances in central European oil markets to pick up any implications for competition between the two major Polish refiners.

4. Ensure competition authority vigilance over the distribution/retailing market

There is scope for the vertical exercise of market power within the franchise sector of the branded distribution/retailing networks of PKN Orlen. The long term contracts that underpin the franchises could be used to exert unfair bargaining power on franchises when they need to be renewed (a small business protection as well as a competition issue). The refiners may also exert market power over the non-branded distribution/retailing sector, through uncompetitive wholesale supply contracts (*e.g.* exclusivity clauses).

- Ensure OCCP vigilance over the vertical links between refining and distribution/retailing. Note that OCCP may need to pay more attention over time to these issues, including small business protection.
  - ❖ If competition issues become difficult, consider structural remedies, including
  - ❖ Specific controls on the exclusivity and/or duration of supply contracts between the refiners and non-branded retailers.
  - ❖ Banning dominant operators in the retail market from extending their networks long enough to allow competitors to develop their networks. Where excess domination exists already adjust the situation by appropriate means (*e.g.* banning anti-competitive restrictions on sales and/or supply contracts).

B.2. THE COAL SECTOR

Background

The coal sector currently plays a key role in Poland's energy supply and is one of the largest in the OECD: but demand is decreasing, costs are high and massive restructuring is needed

Around 65% of Poland's primary energy is sourced from hard and brown coal (50% is hard coal). Its main use is in electricity (55%) which is nearly all generated from coal. Poland is the third largest coal consuming country in the OECD, and Polish output is larger than the whole of the EU. But the restructuring of the economy away from heavy industry and a shift to gas has created a significant downtrend in domestic demand. Coal exports have also decreased in recent years, from 32 million tons in 1995 to 23 million tons in 2000 (Poland remains the largest coal exporter in Europe). The industry has high excess capacity and costs, and is undergoing a massive restructuring.

Hard coal is the focus of the present analysis. At the end of central planning, the sector, which is wholly state-owned, was made up of 70 mines with a capacity of 180 mta (million tonnes per annum), and employed around 430 000 (1 in 40 of all workers). Dramatic problems followed: domestic demand collapsed, and world coal prices faltered, resulting in fundamental problems with the maintenance of financial liquidity, despite some initial restructuring. Further restructuring grouped mines into joint stock coal "holding" companies which took over responsibility for the individual mines in their group. This was followed by the grouping of mines destined for liquidation into separate companies so that the others could focus on business development.

The reforms engaged so far have been successful: they must be followed through

The restructuring process culminated in 1998 with the government programme "Hard Coal Mining Reform in Poland in the period 1998-2002", supported by the World Bank. There are currently 41 productive mines and 25 mines in liquidation. The government programme covers financial restructuring, the closure of unprofitable mines, employment restructuring (with a social package to mitigate unemployment problems), new industrial development in coalfield areas, improving coal industry management, eventual privatisation of profitable mines and environmental rehabilitation.

The Minister of Economy oversees reform. The State Agency for Hard Coal Mining and Restructuring (PARG) reports to the Minister of Economy and is responsible for monitoring the programme's implementation.

In recent years there has been steady progress in many areas. The sector achieved a small surplus in 2000 (though the performance of individual mines varies widely). Overall the programme can be regarded as a substantive success: employment has fallen from unsustainable levels (more than expected) with muted social problems, output has fallen

Table 9. **Hard coal sector: restructuring performance**

	1990	1998	2000
Employment	391 000	208 000	155 000
Output	147 million tonne	116 million tonne	102 million tonne
Productivity (t/man-year)	390	504	627 (estimate)*
Exports	28 million tonne	28 million tonne	23 million tonne
Domestic demand	120 million tonne	90 million tonne	80 million tonne
Prices (average per tonne)		PLN 121	PLN 132
Costs average per tonne)		PLN 144	PLN 130
Losses		PLN 4 248 million	PLN 1 737 million
Liabilities		PLN 16 500 million	PLN 22 100 million
Restructuring expenditure		PLN 1 008 million	PLN 1 650 million

* Germany: 590; UK: 3 200; USA: 11 900; South Africa: 3 900.

back to demand levels, average production costs have fallen and productivity has improved significantly. Around 80% of planned redundancies have occurred. The creation of new employment opportunities has been less successful, with only 900 new jobs. The eventual "steady state" for output is estimated at around 100mta (roughly the present output).

Restructuring has incurred substantial costs (borne by the government budget given state ownership). In the 1998 government programme, subsidies for restructuring of the hard coal sector over 1998-2002 were estimated to be PLN 7.2 billion (1.5 billion for mine closures, and the rest for social, redundancy and environmental purposes). The financial restructuring plan is for the sector's debt to be paid out of profits once it has returned to profitability, though much of the debt will need to be written off and restructured.

Prices were directly controlled before 1990. They were liberalised in several stages from 1992. They are now fully liberalised and negotiated between buyer and seller. By the standards of liberalised markets prices are low for households, comparable for industry. Given the government's continuing aid to the sector, the temptation does exist at least in principle to encourage higher prices which would raise revenues and reduce the aid needed. Privatisation would remove both the temptation and the means to do this.

Excess domestic production (relative to demand) is exported. Export prices reflect the internationally traded price of coal. The EU takes nearly 70% of Polish exports. In 1998-1999 prices were below domestic prices, incurring significant losses for the sector (UK companies complained about dumping). World coal prices are currently quite high, but prices tend to follow a cyclical pattern and are vulnerable to the global economic slowdown. Lower export prices would put the industry under considerable renewed pressure. This underlines the importance of completing the restructuring programme, and possibly considering whether it will be sufficient. The sector is also protected from cheap Russian imports by quota. This is not unusual in Europe, but works against strengthening the competitiveness of the industry by reducing the pressures on it to reduce costs. Ultimately privatisation is needed to promote an effective integration of the Polish hard coal sector with world markets.

Conclusion

The government's reform programme is ambitious but necessary, and has been successfully implemented to date. A number of important challenges remain: the restructuring programme must be completed, privatisation must be taken forward, and the sector must be fully integrated into the international market. The very high unemployment rate in some areas also needs attention.

Recommendations

1. Complete the restructuring programme as currently set out

The programme to restructure the hard coal sector is ambitious and has largely succeeded in meeting its objectives so far. This success, particularly in returning the sector to operating balance in 2000 (at present prices), should not weaken the resolve to continue the programme. There is some way still to go, against a challenging background of high unemployment in some mining regions.

- Complete the "Hard Coal Mining Industry Reform Program in Poland 1998-2002".

2. Assess the sustainability and competitiveness of the resulting industry structure

The objective should be an industry which is profitable, competitive and can hold its own in the international coal market. Currently world coal prices are high by historical standards: should they fall this will put pressure on domestic prices, and could make the industry vulnerable again to big losses. Some further mine closures may be necessary to avoid losses, reduce output and ensure that the industry is profitable and globally competitive.

- Before completing the restructuring programme, assess the sustainability and competitiveness of the resulting industry structure in the context of the global coal industry and market prospects.
  - If necessary draw up a new plan.

3. Pursue privatisation once mines are profitable

Privatisation also needs to be addressed if the industry is to hold its own in the global market. The industry is currently almost entirely state-owned. The privatisation of the Bodganka mine (one of the most profitable) and the Budryk mine is a step in this direction. Privatisation will reduce the exposure of the government to losses from cycles in the industry.

- Once mines have become profitable, pursue privatisation options that will reduce the government's risk exposure and ensure the industry is competitive.

4. Use state aids to restructure the industry: base these on transparent taxes

The industry is currently the recipient of significant state aid for the restructuring programme. It is important that state aids – as well as being justified – should be transparently allocated (*e.g.* using a tax-based mechanism such as a tax on electricity consumption which is paid to electricity generators to compensate for their purchase of relatively expensive domestic coal).

- Make sure that state aids are used to restructure the industry, and are *not* used to subsidise sales. Use transparent mechanisms such as tax transfers.

5. *Ensure that imports and exports meet competitive criteria and are transparently managed*

The price of exported coal – in the Polish context this means coal that is surplus to domestic demand – is set to reflect the internationally traded price of coal. Export prices were below domestic prices and average total costs in 1998 and 1999. This not only revealed that the domestic coal industry – despite much progress – is not yet competitive, but also gave rise to significant losses for the industry. At the same time coal imports from Russia have been severely limited through quotas, to protect the domestic industry.

- Ensure that exports are cost-effective and transparently managed.
- Prepare for a long-run decline and eventual phasing-out of exports.
- Aim for a full integration of the domestic industry with the international coal market, on a competitive basis. Phase out the import quota system gradually.

B.3. THE ELECTRICITY SECTOR

Background

The electricity sector is in the process of liberalisation: much of the legal framework and some of the structures are in place to carry this through

The electricity sector has seen considerable changes since 1989 when reform and commercialisation began. It was then owned by the Treasury and managed jointly with the coal sector. Prices bore no relation to costs but were an instrument of social planning. Significant overcapacity went with generally inefficient and highly polluting plant.

Reform started with the separation of electricity from coal issues, the removal of regulatory functions to the (now) Ministry of the Economy, the creation of around 40 joint stock companies for generation and 33 distribution companies, and the reorientation of international grid connections from Eastern to Western Europe. Grid management and system operation were vested in the Polish Power Grid Company (PSE) which became the "single buyer" for the sector. Large price increases followed. A substantial investment programme followed to update old, inefficient and heavily polluting plant, financed largely by commercial, long-term bank finance secured on the revenue stream provided under long term power purchase agreements (PPAs) between PSE (as single buyer) and the generation companies. Much investment is still needed despite this programme- estimates range up to USD 50 billion.

The 1997 Energy Law was the next major step. It established the Energy Regulatory Authority (ERA), and provided the legal basis for liberalisation of the sector away from the "single buyer" model, to the third party access – bilateral contracting model. Privatisation started in 1998, based on partial privatisation of assets. An updated plan, the "Integrated Schedule of Electric Sector Privatisation", was adopted by the government in April 2001 and revised in April 2002. This provides for an acceleration of the process and continued separation of generation from distribution assets. It is envisaged that the government will maintain ownership of three key generation stations, motivated by energy security concerns. It is further envisaged that ultimately the trading and transmission activities of PSE will be separated and privatised.

The ERA was the first sector-specific regulator in Poland, with a President appointed by the Prime Minister for five years. The President can only be removed in cases of specified serious misbehaviour or incapacity. The President of the ERA is accountable to the Minister for Economy. The ERA employs 285 people and has nine regional offices, a reasonable size. It is responsible for licensing and can impose licence conditions (market entry requirements are quite liberal). It approves and controls retail tariffs for electricity, gas and heat, within the framework of a Ministry of the Economy ordinances. It can waive the obligation to submit tariffs for approval if it considers that the company operates in a competitive market (the aim is to roll back tariff regulation as competition takes hold). The

Table 10. **Electricity access liberalisation timetable**

Date	Annual purchase level (GWh)	Number of eligible customers	Volume (TWh)	% of market open
4 September 1998	>500	21	21.5	21%
1 January 1999	>100	83	37	37%
1 January 2000	>40	180	44	43%
1 January 2002	>10	610	52	51%
1 January 2004	>1	3 300	60	59%
5 December 2005	All	15 million	102	100%

wholesale power exchange market was the first trading area to be exempted from tariff controls. In July 2001 the obligation to submit tariffs was removed from electricity producers and trading companies for wholesale activities. Tariff controls remain on PSE and on distribution companies. The ERA approves the investment plans of the transmission and distribution companies. It enforces quality and safety standards, resolves disputes (notably relating to grid access) and co-operates with the OCCP to act against monopolistic practices.

The tariff ordinance requires that tariffs take account of the need for rebalancing and the "justified costs" of companies, including the cost of development plans. There is a debate as to whether this ordinance allows companies to earn a reasonable return on capital (in other words if it covers investment needs adequately). Transmission tariffs are adjusted every 2-5 years with a CPI-X formula. Decisions are subject to appeal to the Antimonopoly Court (some have been made).

The 1997 law also requires accounting separation for activities, consistent with the EU law. It also sets out a timetable for market opening and third party access to the grid.

The access framework involves regulation of access conditions rather than negotiation between parties. PSE and the distributors are legally obliged to provide access – subject to certain conditions – under the supervision of the ERA, which must approve tariffs. Eligible customers and traders on behalf of the latter can apply for access. The use of third party access is still very limited: as of mid-2001 of 180 eligible customers only 13 had switched supplier, and only 50 access agreements had been made. Access arrangements currently apply to domestically generated electricity, with international liberalisation after EU accession.

The competition law applies to the sector without exception (and has been used: some 20% of OCCP issues concern the energy sector).

Generation is nearly all coal-fired, with a progressive shift to gas expected for heat and combined heat and power (CHP) plants. There are 17 large thermal power stations and 19 CHP plants. Electricity demand is on a upward trend and expected to grow by 41 to 66% between 1997 and 2020, so the new regulatory framework must be capable of providing effective incentives for investment. The structure created so far is pro-competitive with a large number of generating companies. Around 70% of electricity supplied to final consumers is covered by exclusive long term PPAs between the generators and PSE, which run until 2010-2012. Prices under these PPAs are generally higher than market prices. This

is a major issue blocking the evolution of the sector which remains locked in the "single buyer" model unless it can be resolved.

Transmission is in the hands of PSE which is owner and operator of the transmission system, the dominant electricity trader (buyer and seller of power), operator of the system balancing market (necessary for technical reasons in all electricity systems to ensure a balance of electricity on the grid in real time), and responsible for the dispatch of electricity onto the grid. PSE is state-owned and reports to the Treasury. Its mission is to "create, organise, and service a liberal, non-discriminatory wholesale market in electric energy in Poland, including international exchange, and especially to ensure a necessary infrastructure for the realisation of transactions made on this market". In line with its mission PSE will remain sole provider of transmission services and is expected to withdraw from energy trading. This withdrawal is important: PSE cannot be the dominant trader and the neutral provider of transmission services to other traders at the same time. The privatisation of PSE may be considered once the current set of reforms has been carried through.

Some 70-80% of power goes through the transmission system, the rest is purchased directly from local generators including CHP plants. Transmission tariffs do not fully reflect costs yet. Pricing based on the "connection point" principle is planned.

A *power exchange* has been set up: the Polish Power Exchange (PPX) started operation in July 2000 as a voluntary market following the (Scandinavian) Nordpool model. Potential participants include the 36 generators, 33 distribution companies, 41 licenced traders and eligible customers under the liberalisation schedule. PPX is owned by the Treasury and others including the PSE. The market operates on a next day basis, with 24 markets corresponding to each one hour time period for the next day. A futures market commenced in 2001, although trading has so far been relatively limited, and also there are plans to start a current day market. The volume of electricity that can be traded through the exchange amounts to 30%. However most purchasers conclude bilateral contracts. As a result, trading has so far been mimimal, peaking at just 1.5% of electricity consumption. This is not surprising, given an obligation on the distributors to buy electricity generated by CHP and renewable generators located in their distribution region. This means that only some 5% of electricity can be traded, and PSE's balancing market is larger.

Distribution is organised into 33 regional companies, which own and operate the distribution grid and supply power to retail final customers. The distribution companies are required to purchase electricity from PSE in a pass-through arrangement of the latter's contracts with the generators. They are all state-owned apart from the largest southern company, which was privatised to Vattenfall. Privatisation of the remaining companies has started though the government proposes to retain a minimum 25% + 1 share in each privatised company until fulfilment of the investment programme by the investor. Most of the companies are too small to be efficient, and some combination of the companies could occur without raising issues of market power. The *retail* function is currently bundled with the distribution function: the distributors have an obligation to supply customers in their area. They can sell elsewhere but this is infrequent.

Prices are relatively low by international standards, despite the increases. However electricity accounts for around 10% of the average household budget. Some rebalancing is still needed to align prices with real costs, not least between households and industry.

Effective competition will only emerge if the power of PSE at the centre of the market and the problem of long-term contracts are tackled

PSE's role as transmission operator and as the main trader disadvantages other players. The presence of long-term contracts which have "locked in" most electricity sales leaves little room for competitive trading. These are the two major impediments to an effectively functioning market.

"Locked-in" electricity sales account for some 95% of the market, against a potential 43% of competitive sales that could be possible with the legal market opening so far. To raise the electricity volume traded in the free market, particularly the spot market, the government has developed a novel policy to deal with this "lock-in" problem: the "Compensation Payments Scheme" (SOK) under which generators may sell electricity on the open market and receive compensation for any revenue shortfall relative to what they would have got under the PPAs. It is a necessarily complex system and it remains to be seen whether the incentives are adequate for generators to opt into the system. In the pilot phase three long-term contracts were prepared for SOK implementation, but were suspended due to the legal-tax problems. Relevant modifications are expected. One important issue is that SOK is optional: it has to be to respect the privacy of the PPA contracts. If the SOK fails, then the only prospects for competition are from imported electricity or through re-negotiation of the long-term PPAs. To substitute SOK, the MOE is also considering other options such as the possibility to implement a special fund based on charges imposed on end-users. But the expected rise in electricity demand should provide some headroom for generators to start using the competitive market.

The government's policy is for PSE to withdraw gradually from trading as resolution of the long-term contract lock in problem, and retrench to transmission ownership and operation, but without any specific plan or timetable. However, the lack of a clear and mandatory plan for PSE's withdrawal, which the government appears to be leaving to natural attrition, is likely to raise problems. PSE is expected to lose market share in an increasingly competitive market. But, PSE's *de facto* control of the balancing market – which handles larger volumes than the power exchange – raises a conflict of interest. Given PSE's dominance as a trader, since it has both the ability and incentive to influence the relative size of transactions in the balancing market and the power exchange to its own advantage, it may be disinclined to withdraw from trading as a result.

Conclusion

Although a fairly comprehensive legal basis for a competitive market exists (including the establishment of an energy regulator) and a power exchange has started operation, there is very little *de facto* competition yet. The government has correctly identified, and is seeking to address, the issues that need action for competition to take hold. These issues will need to be vigorously pursued. Effective competition will bring one key advantage in the Polish context: it can be expected to mitigate the further price rises that are inevitable in the continuing adjustment to a market driven economy.

Recommendations

1. Continue with the present privatisation plan, maintaining substantial separation of generation and distribution to preserve competition in these sectors

The revised privatisation programme aims to accelerate the process maintaining separation of generation and distribution. Whether such bundling is harmful to competition depends on how structurally concentrated, and hence competitive, distribution and generation will be in their own right. The more competitive, the less likely that vertical linkages will be harmful.

- Press on with the present privatisation plan, but take care to avoid a level of structural integration of generation and distribution which might limit the choice of suppliers and forestall competition.

2. Pursue the proposed system (SOK) for resolving the problem of long-term contracts or otherwise resolve the contract lock-in problem

The long term contracts (PPAs) between the generators and PSE are a major block on the development of a competitive market. The distribution companies are also required to purchase electricity generated by CHP plants connected to their grids. The distribution companies must purchase a proportionate amount of the electricity purchased by PSE under long term PPAs. At present the distribution companies have no effective ability to supply power outside their geographical area, largely because the size of the liberalised market once PPAs are taken into account is so small (also because third party access to the grid is still difficult).

These lock-in contracts are therefore a major issue affecting the prospects for competition. The scheme (SOK) with which the government proposes to resolve it (under which generators may sell electricity on the open market and receive compensation for any revenue shortfall relative to what they would have got under the PPAs) should be pursued.

- Press on with implementation of SOK or PPA renegotiations on the same timetable as the market-opening timetable. Use the government's role as pre-privatisation shareholder if necessary to persuade companies to take part in SOK or renegotiate contracts (subject to creditor approval).
- As SOK or contract renegotiations develop, phase out the obligation on distribution companies to buy power from PSE, and enable them to supply clients outside their geographical area.

3. Address the competition constraints arising from the vertically integrated transmission company: establish an independent system operator or unbundle PSE's trading activities from its other activities

The Polish Power Grid Company (PSE) is the state-owned owner and operator of the transmission system, the dominant electricity supplier and trader, and the system operator responsible for all electricity dispatched on the grid. In a competitive market the trading role needs to be separated to avoid abuse (PSE could favour its own trading activities in operating the dispatch of electricity on to the system, or in transmission services).

A further issue in the effective development of competition is the technical capacity of the current transmission system to manage a multiplicity of supply contracts between numerous traders – the system was designed for just one trader. Solving this issue requires a reappraisal of the current management, ownership and regulation of the transmission grid, including system operation.

- Establish an independent system operator responsible for dispatch (including the balancing market) *or* unbundle PSE' s trading activities from its other activities and privatise these separately.
  - ❖ If these structural measures are not feasible in the near future, ensure that the Energy Regulatory Authority (ERA) limits PSE's ability to manipulate the balancing market to the detriment of competitors and the development of trading on the power exchange.
- Enhance the powers of the ERA to mandate an expansion of the transmission system (for example by requiring PSE to formulate an investment plan for approval, and ensuring that the tariff system recoups the costs).

4. *Rebalance tariffs with a view to completing this before EU accession*

Some tariff rebalancing is needed between the price of electricity and transmission/distribution charges, which vary widely between regions. Rebalancing is also needed between industrial and household consumers. Transmission charges are too high and electricity charges for small consumers are too low. In other words current tariffs do not reflect real costs. This needs to be addressed before competition takes off with EU accession, to avoid inefficient market entry, and "cherry-picking" the profitable market segments. However as electricity tariffs are relatively low by international standards these changes will need to be handled with care.

- Identify and implement a clear plan to rebalance tariffs. Aim to complete this before EU accession.
  - ❖ If necessary – to avoid price shocks caused by the adjustment of tariffs to real costs – consider implementing a transparent subsidy for poor consumers.

5. *Ensure that the Energy Regulatory authority can effectively resolve problems of access to the grid*

The legal framework and timetable for third party access (TPA) to the grid envisages a progressive opening of the market, culminating in full market opening (all electricity customers are free to choose their supplier and access the grid) in 2005. The government has chosen regulated TPA (the grid companies are legally obliged, so long as it does not disadvantage other customers and so long as technical conditions are met, to provide access for eligible customers). The ERA is responsible for resolving potential disputes and approving tariffs for grid access and use. These powers are very necessary: so long as the vertically integrated transmission/trading and distribution/retail companies continue to exist, they are in a position to favour their own supply activities for grid access, frustrate access by others, and to cross-subsidise their supply activities from their grid activities.

However the ERA's effectiveness so far in securing TPA is in doubt. TPA has been very limited. Part of the problem is the difficulty of concluding access contracts due to apparent "technical or legal difficulties", some of which may be due to behaviour by the grid companies to frustrate access.

- Have the ERA take an early opportunity to test its powers to resolve access disputes when "technical limitations" are raised as a barrier to access.

B.4. THE NATURAL GAS SECTOR

Background

Gas market liberalisation is at a very early planning stage

Gas accounts for around 10% of total primary energy supply and its use is expected to increase. Around half the population is connected to gas. Industrial use is more significant, the biggest user being the fertiliser industry. There is so far hardly any use of gas in power generation.

Domestic production accounts for some 35% of demand, but Poland is mainly dependent on Russian imports. The prospects for further domestic production are relatively modest. A key government objective is import diversification, through Norwegian and possibly Danish gas. There are five border connection points – a expansion of the international connections is planned – and a major transit route for Russian gas exports to Western Europe (the Yamal pipeline) goes through Polish territory.

Box 10. **The structure of the natural gas sector**

The functional classification of the gas sector is as follows:

a) Production – which can be further broken down into the exploration, drilling, extraction and processing of gas. For this paper, liquefaction plants and re-gassification facilities for gas in its liquid form (known as LNG) are included in this stage of production.

b) Import: negotiation and execution of gas import contracts. The national company has generally the exclusivity for imports

c) Transmission – the high-pressure transportation of gas to high-volume customers such as distribution companies, large industrial customers and power stations.

d) Distribution – the low-pressure distribution of gas to small and medium-volume gas customers.

e) Storage – the smoothing of the flow of gas through the transportation network by pumping gas into holding facilities at off-peak times, and withdrawing the gas at peak times.

f) Retailing and Marketing – the provision of services of contracting with production, transmission and distribution companies on behalf of gas customers and associated billing and metering services.

The Polish Oil and Gas Company (PGNiG) is the main market player. It is a vertically integrated monopoly in imports, transmission (including system balancing), storage and distribution. Around 40% of demand is supplied directly from the transmission system and the rest goes through the distribution system. PGNiG was transformed in 1996 into a state-owned joint stock company (it was created in 1986). Internal restructuring started in the same year, involving commercialisation and a staged separation of the different activities: technical and non-core activities, exploration and extraction, transmission and storage, and (prospectively, the plans are still on paper) the horizontal separation of distribution (which will remain bundled with retail supply). All these activities remain for the present under the ownership of PGNiG. A restructuring and privatisation plan is underway but key details such as whether distribution will be unbundled from transmission are under review by the new government and are not yet settled. According to the original reform programme (being reconsidered at present), apart from transmission and storage, the other functions were expected to be privatised by 2004. Storage – important for system reliability but also needed potentially by new market entrants – is quite limited and needs upgrading.

The 1997 Energy Law regulates the sector, and the ERA has the same regulatory powers as in electricity. A number of licences have been granted to traders. The regulation of exploration, exploitation and storage within depleted gas resevoirs is with the Ministry of the Environment. A 1998 ordinance sets out a market opening schedule which started *de jure* in July 2000, under which large customers have potential access to the grid and are free to choose their supplier. But no decision has yet been made on the framework of grid access –whether it should be regulated or negotiated. A framework for access to storage also needs to be put in place. No actual access arrangements have yet been implemented, and just one agreement concluded. Market opening is currently restricted to domestically extracted gas but there are plans to open up in conformity with EU law.

A number of developments are needed for competition to take hold: the two key ones are the effective restructuring of PGNiG and import liberalisation

PGNiG restructuring – the effective disaggregation of potentially competitive activities – is essential. The number of distribution companies and their eventual ownership are very important for the prospects of competition in the retail sector. Fewer than four companies would damage prospects, and privatisation to different owners is also important, so that the companies can challenge each other on their respective territories. The OCCP will need to monitor the future market structure to prevent consolidation. The entrance of gas traders should help to open up the field, if they can gain effective access to the distribution grids. This is turn depends on effective access and tariff regulation by the ERA. Import liberalisation will be a great help in stimulating competition in this potentially difficult environment.

There are other important issues in the way of competition. As with electricity there is a need for tariff rebalancing (which needs to be linked to the tax regime), which will raise prices considerably. The government does not have a timeframe for this, but EU accession can be expected to drive it, as competition will make cross-subsidies between customer groups unsustainable. Long term contracts which cover imports are an important impediment to the development of competition and difficult to undo because of the risk to PGNiG's financial solvency. But the expected increase in demand should help to open up opportunities for new market players. Access to the grid must be tackled by the ERA through careful regulation, preferably within the framework of a regulated access regime,

and a stronger approach to separating the different activities of PGNiG – especially transmission from the rest including imports, sales and storage – so as to remove both the incentive and the ability to discriminate against competitors in grid access. Regulatory functions could be streamlined to ensure that operational and access issues relating to storage are with the ERA.

Conclusion

The gas sector is at a very early and preparatory stage of reform. Some progress has been made in laying the groundwork for restructuring PGNiG but this programme needs to be implemented. If the programme – including privatisation – is completed effectively so as to make a clear separation between transmission and other functions, the new structure should be effective in encouraging competition. But it needs to be accompanied by measures to diversify supply sources, both for security and competition purposes, which requires significant infrastructure investment and an increase in storage capacity. Import liberalisation will greatly help market opening and this process should not be delayed.

Recommendations

1. Proceed with the planned restructuring and privatisation of the industry

The separation of PGNiG is still on paper, yet to be implemented and is being considered by the new government. The government also has plans, yet to be finalised, for privatisation. The restructuring plans are reasonably well conceived to set up a market structure conducive to competition. But progress is at a very early stage, and care must be taken to avoid problems: a critical mass of at least four independent distribution companies is necessary to stimulate competition in supply, and vertical links between production and transmission should be avoided.

- Proceed with the privatisation and restructuring plans.
  - Sell the distribution companies to separate investors over the next four years.
  - Privatise the transmission and storage company as soon as possible.
  - Take care to consider the competition consequences of upstream vertical integration.
  - Distribution companies should be able to supply clients outside their geographical area.

2. Ensure that transmission activities are quickly and effectively separated from other activities

Pending the privatisation of PGNiG's transmission activities, it is important to ensure that transmission is effectively separated from other activities, in particular imports and supply. As with PSE in electricity, PGNiG's roles as a provider of transmission services as well as supplier of gas give it the opportunity to frustrate access to transmission access by others, and to favour its own supply activities.

- Pending privatisation, operationally separate transmission activities from import and supply activities, and establish a gas system (dispatch) operator.

3. *Consider divesting storage assets to create a competitive market in storage services*

Storage is needed to maintain a balanced flow of gas in the pipeline network through peak and off-peak periods, and to provide a security cushion for meeting unexpected demand or shortfalls in supply. Access to storage is therefore needed by gas suppliers. As it is not generally a natural monopoly there is scope for competition in storage services. PGNiG's current monopoly of storage, and the fact that storage capacity is limited, raises the risk that new suppliers will find it difficult to access storage services.

- Consider divesting enough storage assets to create a competitive market in storage services, to assist market entry for gas traders and suppliers, taking care at the same time to cover security needs (the use of stored gas for emergencies) through regulation.
- In the absence of divestiture, careful regulation of access to storage will be necessary to provide a basis for new entrants into the wholesale market – otherwise PGNiG will be able to foreclose entry.

4. *Take forward tariff rebalancing*

The ERA must approve gas tariffs, on the basis of justified costs (including the cost of delivering gas and of necessary infrastructure investment), of the need to rebalance tariffs so that they reflect real costs, but also of the need to protect customers from unjustified increases and of price shocks**,** which limits the pace of rebalancing. Rebalancing gas prices to reflect costs will generate a substantial rise in prices (for households mainly). But the limit on tariff increases has generated losses for PGNiG and held back necessary investment. However market liberalisation (with EU accession) will put a *de facto* time limit on the disparity between tariff and costs, which cannot be sustained under competition. But it should also mitigate the increases as competition can be expected to raise efficiency.

- Consider setting out, publicly, a multi-year plan to complete rebalancing, so as to provide greater certainty for market participants, and a better information base for the important investment decisions that need to be made by prospective participants in the privatisation plan.

5. *Ensure that any future long term contracts are justified as essential for security reasons*

PGNiG has long term take or pay contracts (which are understood to have a 25 year term and to provide for significant volume increases) which cover nearly all imports. Its contracts with major customers, including the envisaged distribution companies, contain partial "pass-through" of these take or pay obligations. Such contracts limit future competition but may he difficult to undo, not least because the solvency of PGNiG would be put at risk. Fortunately there is still scope for competition based on domestic production (some 34% of demand), and the government has specific objectives for diversification of supply. New more flexible supply contracts could meet the growth in demand, helped by liberalisation of transmission access, including for imported gas.

- Ensure that PGNiG avoids entering into further long term contracts that are not essential for security purposes, so as to protect and maximise the scope for new market entry.

6. Complete the regulatory framework for access to transmission, distribution and storage services

A schedule to open the market and liberalise access to transmission and distribution has been established. However market opening is currently limited to very large customers, in respect of domestic gas only. And the regulatory framework for access is not yet fully in place: in particular no decision has yet been taken whether access should be negotiated, or regulated (*i.e.* mandatory as it is for electricity). Only one access agreement has been concluded and no actual access implemented. Competition cannot develop without effective access by new suppliers to the transport of gas. Access to storage services is also essential. Access to infrastructure facilities for imported gas is also very important to encourage new market entrants, and in the context of EU accession which will accelerate market opening.

- Complete the regulatory framework for access to transmission, distribution and storage services, opting for regulated access under the authority of the ERA.

7. Liberalise access to transmission for imported gas as soon as possible

Access to infrastructure facilities for imported gas is also very important to encourage new market entrants, and in the context of EU accession which will accelerate market opening.

- Aim to remove import restrictions, and to treat imports and domestic gas the same, from the date of EU accession.

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PART II

Chapter 6

THE TELECOMMUNICATIONS SECTOR*

* For more information see: "Background report on Regulatory Reform in the Telecommunications Industry" available at *www.oecd.org/regreform/backgroundreport*

Background

Poland has taken some modest steps to liberalise and restructure its telecommunications sector

The Polish telecommunications market remains in the hands of relatively few operators, notably the original monopoly incumbent, Telekomunikacja Polska S.A. (TPSA). In fixed telephony, the local service is typically a duopoly (except the Warsaw area), while the long distance market has only recently opened up with three new operators. On 1 July 2001 the first alternative operator – Niezalezny Operator Miedzystrefowy (Independent Inter-zone Operator) started providing services on a per-call carrier selection basis. It captured an estimated 15% of the long-distance market in its first four months of operation. In March 2002, after opening the long-distance telephony market, the President of URT granted another three licences for new operators. International service remains a TPSA monopoly until 2003. Three companies have been competing in the mobile sector since 1996.

The liberalisation process started with the 1990 Communications Act and disaggregation of the original post and telecommunications company to create TPSA and Polish Post. TPSA's monopoly of local services was abolished in 1992. A second phase was engaged with an amendment to the Communications Act of 1995 which set up a regulatory regime of licensing for the provision of telecommunication services by tender. A regulatory regime for interconnection agreements was also set up. Privatisation of TPSA began. TPSA was put under the control of the Treasury, and some shares were sold in 1998 and 2000. A third phase began with the adoption of a Telecommunications Law in 2000 (replacing the part of the Communications Act dealing with regulation of telecommunications), which simplified market entry procedures, abolished the foreign ownership restriction on operators apart from international service until 2003, provided for unrestricted competition from January 2003, created an independent regulator, the Office of Telecommunications Regulation (URT), and provided a definition of universal service as well as a framework for its provision. The Law sets a framework for most of these issues but secondary legislation (ordinances) is required to give them effect.

Market structure and competition has progressed a little but TPSA remains the dominant player by far in fixed line services

There are currently 56 public telephony service providers (many have a wireless local loop) and a number of cable TV operators, some of which provide Internet access services. TPSA remains the dominant player: it retains in particular the lion's share of the local fixed line telecommunications market (competitors had just 6% of the market by 2000). Nevertheless from 1996 a duopoly market structure has evolved for local services in rural areas and small cities (despite the fact that local operators had to offer public payphone services and invest in network extension). Fixed line telephony penetration in Poland is

Table 11. **Structure of the Polish telecommunication market (December 2001)**

	National providers	Regional providers	All providers
Local telephone services	1	52	53
Long distance services	4		4
International services	1 (TPSA monopoly)		
Mobile	3		3
Wireless local loop			40
Paging			3
CATV			569
Data services			404
Internet access			693

Source: The Office of Telecommunications Regulation (The URT).

Table 12. **TPSA's local telephony market share (Number of subscribers)**

1995	1996	1997	1998	1999	2000
100%	100%	97.97%	96.33%	94.72%	93.43%

Source: The Office of Telecommunications Regulation (The URT).

28%, very low by OECD standards, and much lower than other central European countries. TPSA's continued market dominance is holding back fixed line telephony penetration.

Mobile telephony is in better shape. It is growing faster than any other telecommunications sector and helping to bridge the gap between demand and supply for fixed line services, albeit at much higher prices than if fixed line services were more widely available. The number of mobile telephony subscribers (including pre-paid) exceeded 10 million in December 2001, up from 1.93 million in 1998. The three operators are Centertel, PTC and Polkomtel.

Table 13. **Mobile operators and their current ownership status**

Operator and market share	Ownership status (as in December 2001)
PTK Centertel (23%)	Telekomunikacja Polska SA (66%), France Telecom (34%)
Polkomtel S.A. (36%)	Polski Koncern Naftowwy ORLEN SA (19.61%), KGMH Polska Miedz SA (19.61%), Vodafone Americas Asia Inc. (19.61%), Tele Danmark A/S (19.61%), Polish state power grid PSE (16.05%), Weglokoks SA (4%), Tel-Energo SA (1.01%), TelBank SA (0.50%)
Polska Telefonia Cyfrowa (41%)	Elektrim Telekomunikacja sp. z.o.o. (47.9998%), Deutsche Telekom (22.5%), Media One International (22.5%), Polpager sp. z.o.o. (4%), Carcom sp. z.o.o. (1.9%), Elektrim Autoinvest SA (1.1%), Elektrim SA (0.0002%)

Source: The Ministry of Posts and Telecommunications (2001).

TPSA is being gradually privatised. 15% of its shares were sold in a first phase in 1998 by public offer (25% was the original target). The proceeds of USD 0.9 billion – the largest in an eastern European privatisation at that time – were destined for social welfare reform. 15% of TPSA's shares were at the same time given to employees. Further steps were taken in 2000 and in 2001. 35% of remaining shares were sold in 2000 to France Telecom Consortium and Kulczyk Holing for approximately USD 4.3 billion, a process in which the government had to remove the foreign ownership restriction and promised to give the winner one of the mobile service licences. In September 2001 an agreement was signed for the sale of a further 12.5% of shares (the agreement also provided for the sale of 2.5% + 1 share for the benefit of France Telecom Consortium until the end of 2002). TPSA's international service monopoly remains intact until January 2003.

Revenue maximisation was one of the main objectives of privatisation of TPSA to the considerable detriment to developing competition in the market. The incumbent was strengthened by the deal before the market was fully opened or restructured for effective competition (despite the fact that the low telephone penetration rate would allow TPSA and others to grow together in a competitive market). The substance of TPSA's privatisation contract with France Telecom was not made public, a lack of transparency which is not helpful and creates uncertainty in relation to future structural and regulatory actions. The privatisation of TPSA should have led to further competition in the telecommunications market, but this did not happen.

An independent regulator has been established, but the Minister retains an important role: the balance is not yet right

The Communications Act of 1990 separated responsibility for regulation from the market players. The *Minister of Posts and Telecommunications (now the Minister of Infrastructure)* was made responsible for policy and regulation. The establishment of the *Office of Telecommunications* (URT) with the 2000 Telecommunications Law was a significant change, in which some responsibilities were transferred to the new regulator. However, under the Telecommunications Law the Minister remains responsible for the promulgation of executive provisions (ordinances), *inter alia* for setting out the framework and details of the authorisation and permit regime for market entry, specifying the detailed requirements for universal service, developing the criteria for assessing an operator's market share (which determines the regulatory regime to be applied), designing standards for meeting interconnection obligations and the development of the interconnection regulatory framework, and elaborating requirements for the management of numbering resources.

Many of the Ministry staff were transferred to the URT. Ministry staffing has been gradually reinforced* but the ordinance work is still delayed. In April 2001 the Minister of Communication promulgated an ordinance on the detailed criteria for establishing operators' market shares in individual services and the methods to be used to determine such shares. This regulated the definition of telecommunication service markets, the basic criteria for establishing operators' shares in telecommunication service markets, auxiliary criteria for establishing operators' shares in telecommunication service markets and the basis on which operators' shares are calculated.

* The two departments in the ministry responsible for telecommunications policy and the preparation of ordinances to give effect to the Telecommunications Law now have over thirty staff.

The *URT* was established in response to the need to conform with relevant directives for EU accession. It has now been replaced by the *Office of Telecommunications and Posts (URTiP)* which has taken over all the duties of the URT. The President of URTiP reports to the Ministry of Infrastructure. Since 1 April 2002, he is appointed by the President of the Council of Ministers, upon a motion of the Minister of Infrastructure, for a five year term, and cannot be dismissed except under exceptional circumstances. The URTiP can impose fines (up to 3% of a firm's revenues) and penalties to enforce its decisions. It is responsible *inter alia* for issuing and revoking authorisations and permits for telecommunications services and equipment, the award of frequencies, co-operation with the OCCP in designating operators with a dominant position or significant market power, issuing criteria for universal services, interconnection and leased-line services, arbitrating in disputes over interconnection and leased line services, and the assignment and withdrawal of numbers. But its powers are limited to the enactment of regulations within the framework developed by the Ministry, and (from 1 April) the President can, within his competencies, develop the drafts of ordinances delegated to him by the Minister. The URTiP does not have the power to issue the regulations to give effect to the general principles set down by the Law. This is unlike most other OECD countries and severely curtails its ability to take action to create the conditions for competition. The Constitution, which requires that ordinances and regulations be issued by Ministries alone, appears to be a block against giving it wider powers.

The former National Radio Communication Agency (PAR) and the National Posts and Telecommunications Inspection were consolidated into the URT, which has around 750 staff and 16 regional branches. This is rather large, and its management could be distracted from the key function of creating the conditions for effective competition. Some aspects of radio spectrum management could be hived off to streamline the URT's role. And it needs to build up staff expertise in regulation, such as interconnection issues.

The *Council of Ministers* is also heavily involved in policies and actions which guide the evolution of the telecommunications sector. It played a crucial role in determining the pace of privatisation and the structure of TPSA. Its President determines the National Frequency Allocation Table. The Council can determine whether the current TPSA monopoly on international services can be lifted before 2003. The OCCP plays an advocacy role for competition and enforces the general competition law in telecommunications, which is not subject to any exemptions. It played an important role investigating monopolistic practices before the URT was set up.

Other bodies are involved in the regulation and development of the telecommunications market. A *Telecommunications Council* exists as a consultative and advisory body to the URT President on issues relating to universal service, interconnection, frequency management, and compliance with electromagnetic requirements. The *National Council of Radio Broadcasting and Television* reserves the frequencies for broadcasting companies, oversees the licensing allocation process and issues licences for radio and TV broadcasting, in consultation with the URT.

Telecommunications regulation needs to be significantly developed if it is to be effective in developing competition

The Telecommunications Law which was adopted in July 2000 took effect in January 2001. The main drivers were the need to conform to the needs of EU accession and

the need to meet WTO commitments. EU directives on telecommunications require access to basic telecommunication services at affordable rates and an independent regulatory body. "Open Network Provision" (ONP) also requires that new entrants can gain access to dominant operators' networks at every technically feasible point and at cost-based prices. But key parts of the Law need to be given effect through secondary ordinances.

The Law removed many of the restrictions to fuller competition and laid a legal basis for the creation of a competitive environment. But it contains a key exemption: TPSA retains its international services monopoly until 2003. An important change is the abolition of licensing, replaced by authorisations. The URT together with the OCCP are empowered to determine which operators have a dominant or significant market position. Such operators must meet certain requirements relating to interconnection, co-operation between operators, prices, terms and conditions, and offers concerning universal services and leased lines, all aimed at limiting monopolistic practices and protecting consumers.

Entry and licensing

The Law lifted restrictions relating to foreign ownership and the acquisition of individual TPSA shares established by the 1990 Communications Act. The URT and OCCP may require information disclosure on the acquisition of shares, and in some cases approval by the OCCP, where issues of concentration may arise.

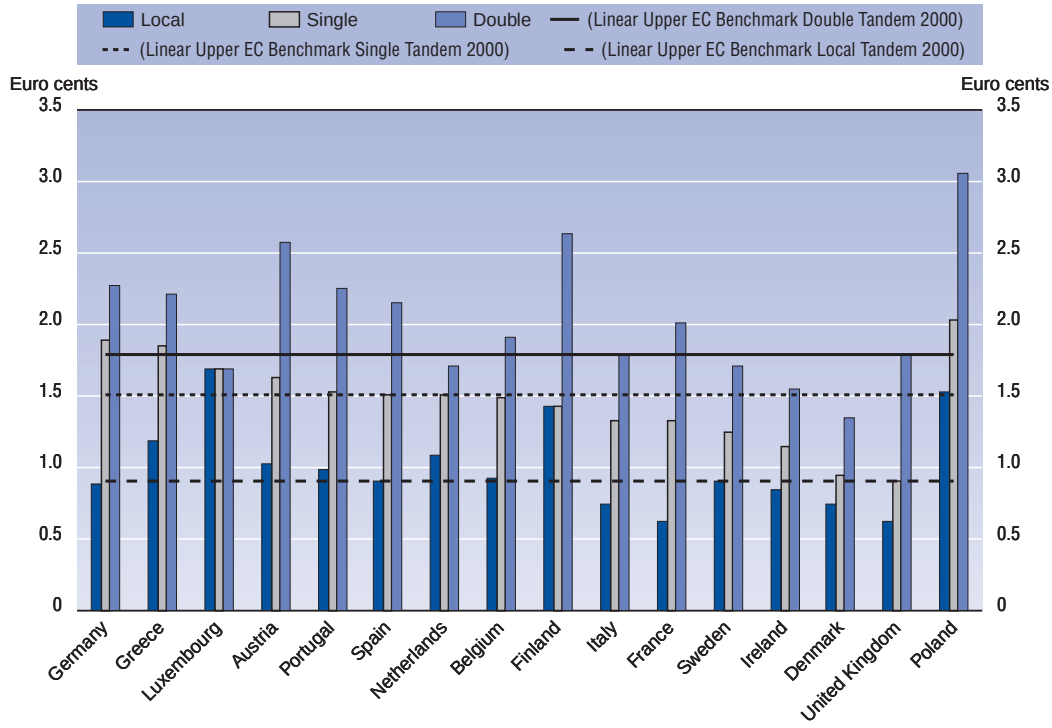
The licensing system was overhauled by the Law and replaced by authorisation and registration procedures. Public telephone services requiring the use of numbering resources spanning an area greater than a gmina (municipality) require an authorisation, the remainder just require registration. The URT issues tenders for activities using frequency resources. However market players with dominant or significant market power have individual licences in which their obligations are spelt out. High tender and licensing fees have been removed, except for activities requiring frequency resources (intended to reflect costs). This will be helpful to new market entrants. However some vagueness remains over market entry conditions. The new authorisations are equivalent to licences in that conditions may be attached, but what these could be is not spelt out. A class licensing or general authorisation regime with clearly expressed general criteria that need to be met would be better. The Minister may set out by ordinance the principles on which the conditions stipulated in authorisations may be modified. Authorisations may be withdrawn only for reasons stipulated in the Law, with URT being the competent authority to decide on the withdrawal or imposition of restrictions on authorisations.

Interconnection

Competition in telecommunications markets crucially hinges on effective interconnection which enables different operators to provide their customers with a service without owning all the necessary infrastructure (fixed line infrastructure at the local access or loop level in particular is not cost-effective to duplicate). Early regulation was not effective in achieving this, because it did not impose any specific requirement on TPSA. A 1999 interconnection ordinance would have provided equal treatment of operators but was not implemented.

The new Law mandates the Minister of Infrastructure to issue the ordinance on detailed interconnection requirements, setting out requirements for interconnection and co-operation between operators and recommending non-binding interconnection rates. .

Figure 1. **Comparison of EU and Polish peak interconnection rates**



Note: The figures are compiled from the EC's "Sixth Report on the Implementation of the Telecommunications Regulatory Packages", December 2000 and the data on interconnection charges by the Ministry of Posts and Telecommunications of Poland.

The Law mandates the use of cost-based interconnection charges. The task of working out the methodology separating the accounts (networks from services) of dominant operators is the responsibility of the Public Finance Minister. The URT has more limited responsibilities and is the executor of ordinance provisions as well as the provisions of the Law. It may require a justification of the costs of interconnection from dominant operators, and operators with significant market power require its approval for their interconnection offers in respect of universal and leased line services. If an interconnection agreement cannot be reached, URT may arbitrate either on its own authority or at the request of one of the parties. These arrangements are not effective either. Poland's interconnection charges exceed EU benchmarks.

Price regulation and rebalancing

Price regulation has traditionally been very light-handed. For example, TPSA's international telephone service rates, determined in consultation with the Ministry, have not been reduced for several years despite global cost changes in this sector. And the Ministry did not impose price ceilings on any operator between 1990 and 2000.

Under the 2000 Law the Minister retains the main responsibilities. The Telecommunications Law gave the URT certain powers with regard to the verification of the tariffs of dominant and SMP operators. The URT may veto specific tariff or modifications, if they contradict the provisions of the Telecommunications Law, which cannot then enter

into force. The Ministry is responsible for setting detailed universal service price regulations (through ordinances, not yet promulgated, to flesh out the Law). Article 35 of the Law states that "prices for telecommunications services shall be set based on transparent and objective criteria, ensuring an equal treatment of users". The Law generally requires that a dominant operator must structure its prices based on costs, and forbids below-cost pricing. These are good principles but the regulatory framework falls very short of ensuring this happens and of restraining anti-competitive behaviour by companies which are dominant or have market power. These companies can still easily set prices to disadvantage potential rivals and impose excessive charges on consumers.

Tariff rebalancing is needed to bring retail prices closer to costs and eliminate cross-subsidies between local calls and subscriber charges, and long distance and international calls. TPSA started to do this from 1998, but has been held up by a lack of knowledge of the costs for different services. It started work on a cost-allocation system in 1999 but its first model for interconnection charges based on this work (using historical costs) was rejected by the Ministry. The OCCP in 1998 asked TPSA to rebalance its tariffs by January 2003. It has also taken action against TPSA: it fined the company PLN 54 million in 2001 for excessively high long distance charges (but did not say how rebalancing should be done). Rebalancing is important: the current tariff structure impedes competition and local operators complain of low local rates (11), used by TPSA to squeeze the new entrants' profits. The 2000 Law contains an important provision: until 2004 it prevents the URTiP from checking whether universal service prices provided by TPSA are cost-based (so as to allow time for the development of an appropriate cost formula for URTiP to check if TPSA has acted correctly, on a cost basis).

Accounting separation

Dominant operators are required to implement accounting separation so that their costs can be matched to tariffs for services in which they are dominant (such as leased lines). It is especially important for controlling TPSA's market power, because (despite being a relatively weak system of control compared with operational separation of activities or even divestiture) it should help to prevent TPSA from subsidising its local service tariffs with revenues from long distance and international services. The government must ensure that accounts are effectively separated so that any cross-subsidisation can be checked by an independent accounting firm. EU experience is well developed and can help to guide the adoption of best practices in Poland.

Alternative infrastructure

Entry into the cable TV market is subject to authorisation, and a permit to build the network must be obtained from the local government. The URT is responsible for regulatory issues. Without specific encouragement, the cable TV market has grown quite fast and there are a number of companies. The largest has been acquired by a Dutch company, which established UPC Polska to deliver telecommunications services together with Internet and cable TV. The company delivers programmes to eight of the ten largest cities, and has launched a broadband Internet service. In the EU, CATV has promoted competition by offering an alternative to the public telephone network. Two problems stand in the way of this competition in Poland. The cable operators have to use the TPSA

ducts, and TPSA can refuse this for the delivery of Internet services and data transmission. And authorisation is needed to deliver services to more than one building.

Minimal regulation of Internet Protocol (IP) telephony can also help competition and innovation. One operator (PTC) started a service in 1999, circumventing TPSA's telephone network, but was declared illegal by the Ministry in 2000 in the context of maintaining TPSA's monopoly in international voice services as support for the share sale. However there is no final ruling as yet: the Ministry and URT are considering what final policy to adopt.

Numbering and number portability

Substantial reform is needed for the current numbering framework. It cannot accommodate the provision by fixed line operators of fixed-to-mobile services. Mobile operators cannot expand their services because of number exhaustion. Generally, operators who want new numbers cannot get them. An ordinance to reform the framework is in preparation by the Ministry. This ordinance will liberalise access to numbering resources and will remove the artificial difference between the division of the country for the award of numbering, and the administrative division of the country. Another concern is the regulatory framework: the Ministry determines the national numbering plan, and the URT assigns numbers according to the plan (in most OECD countries the former role is with the regulator). Also the 2000 Law gives operators the authority to assign numbers instead of the URT.

Number portability (keeping the same number when switching supplier) also needs to be regulated to ensure a level playing field for competing suppliers. If customers cannot keep their number when they change supplier, they can incur significant costs as well as inconvenience. The 2000 Law has no specific provision, apart from noting the possibility of including number portability in interconnection agreements. One of its provisions confuses number portability with number mobility (keeping the same number from the *same* operator when changing address). The Ministry proposes implementing number portability by 2003, following complete network digitisation. But there is no reason to wait this long: number portability can be introduced as soon as it becomes technically feasible. The URT should be responsible for overseeing the process. There are no plans for mobile number portability.

Carrier selection and preselection

The liberalisation of long-distance service has offered subscribers the ability to choose their long-distance operators. This is done by dialing a selected operator access code or by pre-selection only with regard to TPSA's long-distance service. The opening up of long distance markets raises the importance of carrier (operator) selection. This is currently done in Poland by dialling a prefix specific to the carrier. This tends to favour use of TPSA which is accessed without a prefix.

Spectrum allocation and licensing of mobile operators

Licences are required for mobile services. Frequencies must be allocated as part of this process. The URT now has responsibility for allocating frequencies to mobile operators,

through a competitive tender. The allocation process for wireless local loop is not clear: it appears to work on a "first come first served" basis.

A tender process was launched for five third generation (UMTS) mobile licences in 2000. The terms of the process raised objections from the incumbent operators that the number of licences offered was too big, and that new entrants could roam over their GSM networks. The tender attracted just three bids and was cancelled. By default, the incumbents were awarded the new licences, with payment terms stretching to 2022. A further twist to this awkward story was the government's undertaking that TPSA's mobile subsidiary should have one of the licenses, which allows the strategic investor in TPSA to acquire a 3G mobile service license without a bid.

Rights of way and local loop unbundling

The 2000 Law gives operators rights of way over private and public land to install and operate telecommunications equipment. But it is not very effective. Despite the provision, operators must go through individual negotiations with municipalities and private property owners. The URT does not have the power to impose rights of way. An ordinance is needed to set up a dispute resolution mechanism, which does not exist yet. The Law provides for co-location, with the important exception of facilities for voice telephony, which will slow entry into the local market and hold back needed investment.

The 2000 Law does not have any provisions directly related to local loop unbundling. The Law's reference to collocation is vague and insufficient. The success of Internet high speed broadband telecommunications services depends on unbundled access to the local loop. Given that TPSA is already providing DSL services, it is urgent that new entrants are not placed at a disadvantage. There is no evidence to show that unbundling would slow down infrastructure investment. On the contrary, it would give new entrants rapid access to revenues that could be deployed to upgrade the network, and TPSA an incentive to invest in order to maintain its customer base. It can be expected to accelerate the provision of broadband services.

Quality of service

The URTiP monitors the quality of telecommunications facilities and network operation. Six service quality parameters are currently covered: repair effectiveness of faults, call drop rate, fault repair type, number of faults, public payphone penetration, and average access time to the network. But the data has not been published. A new ordinance is expected under the 2000 Law, covering detailed requirements for universal service provision. The URTiP must publish an annual report on its quality. The Law also covers operators' liability towards its clients and the option of litigation if a service was improperly or not performed. The relevant ordinance provides for a two-instance claim procedure, with the option of recourse to the courts, where a claim had been rejected. It stipulates detailed deadlines for reply to customer claims. However the URTiP should have a mechanism to address the performance of operators (both fixed line and mobile), and the option of penalties if operators do not meet requirements. More information on service quality should be published.

Universal service obligation

Universal service is generally defined as providing basic telephone services at affordable rates to residential customers without geographic distinction. The 2000 Law

defines it as synonymous with public fixed line telephony services provided by the public operators – telephony, facsimile and data transmission in the voice waveband – together with directory information, facilities for the disabled, and itemised billing on request. It must be available to every user, countrywide, and cannot be suspended by one operator until it has been taken over by another. Public operators with significant market power will be required to provide universal services at cost-oriented prices, but only from 2004. Currently the universal service obligation lacks clear deadlines and terms and conditions for providing connections: in their absence, the OCCP may be called upon to decide these controversies where they raise issues under the Competition Act.

This framework gives rise to a number of problems. The definition of universal service seems to assume that it is already available. But Poland has a very low level of telephone penetration. This inadequate starting point, combined with the requirement on all fixed network public operators to provide universal service, acts as a powerful disincentive to market entry. The effectiveness of the obligation is also questionable. The operators have no deadline for providing universal service: this is subject to negotiation with the users. This reduces the incentive for systematic further investment in the network. And the fact that the requirement for cost-oriented pricing by operators with market power does not apply until 2004, together with the fact that the dominant operator (TPSA) does not bear a proportionately larger burden than the others, delays the establishment of a level playing field for competitors.

Finally, the funding mechanism's link with the access deficit is neither evident or effective. The shortfall between the revenue from TPSA's charges for connection to the local network and the cost of investment to develop and strengthen the network for universal service is intended to be met by a charge on the other operators for interconnection. But there is no mechanism to require TPSA to use these funds to invest in the network. A much better approach based on international best practice would be to set up a universal service fund for network investment, levied on the public operators.

Competition law

There is no special exemption for the telecommunications sector from the competition law. The OCCP played an important role promoting competition before the creation of the URT. It dealt with issues such as prices, tariff structures and interconnection agreements. Over 70 cases were reviewed between 1990 and 2000. The OCCP considers the overall market behaviour of TPSA unsatisfactory. The main target has been TPSA's behaviour with other operators such as delaying the conclusion of contracts for interconnected billing, charging excessive fees for leased lines, obstructing connection to its network, and cross-subsidising its tariffs. TPSA was fined a record PLN 54 million for an anti-competitive tariff structure: it did at least lower its rates as a result.

Some clarification between the OCCP and URT concerning areas of competence and co-operation may be needed (it may be necessary to confirm that same terminologies and definitions are used between the two institutions).

Convergence

The technological, infrastructure and service convergence of telecommunications, broadcasting, information technology and content sectors raises an important policy

challenge. Inappropriate regulation based on traditional sectoral divisions obstructs the evolution of new services. The Ministry and URT have not taken any action over this. The National Broadcasting Council continues to regulate the broadcasting industry. It considers the content of CATV broadcasting services, leaving other issues with the Ministry and URT. The government should consider unification of the Council and the URT.

The performance of the Polish telecommunications sector is still very weak

The slow start of competition reduces potential growth not just of the sector but of the whole economy. The telecommunications market accounted for 4.4% of GDP by 2000, up from 2.5% in 1996. In revenue terms it has grown at around 15% per annum since the second half of the 1990s. However Poland has a long way to go in providing fixed line services to all. *Fixed line penetration* is very low, even by the standards of other similar central European economies, at just 28 per 100 inhabitants. Poland had 1.8 million people waiting for a connection in 1998 (more than twelve times higher than its nearest "rival", the Czech republic). Benchmarks set by regulators in neighbouring countries to boost fixed line penetration have not been used in Poland, although it requires faster network expansion to catch up. Expansion is unlikely without targets and a regulatory framework that encourages investment. The promotion of duopoly competition in local markets has not stimulated network investment. At the same time TPSA's revenues have grown strongly without a corresponding growth in investment.

This underlines the fact that the current regulatory framework is in urgent need of attention to boost effective competition that would encourage investment by TPSA and other operators.

The mobile sector has performed much more strongly. *Mobile phone density* rose from 0.6 lines to 26.1 lines per 100 people between 1996 and 2001. It is set to overtake the fixed line sector in terms of subscribers by the end of 2002. Prepaid subscribers account for nearly 25% of the market.

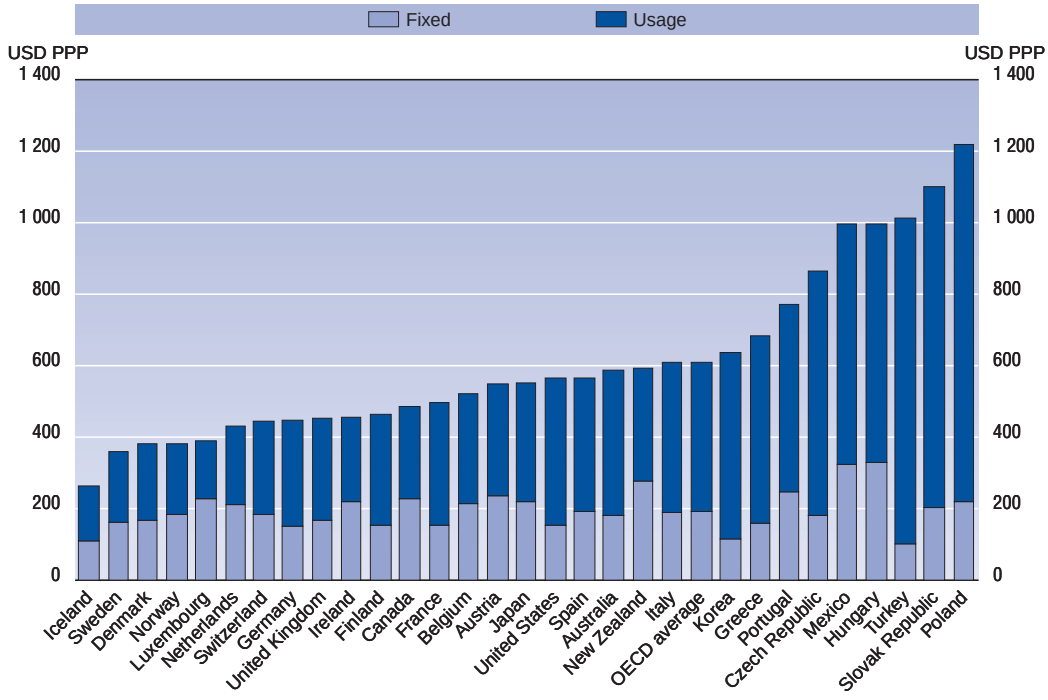
Poland's *prices* are also high relative to other OECD countries, especially for the residential market. The business market fares little better, with Poland the fourth most expensive country in the OECD. International charges have not come down as they have elsewhere, and Poland is the third most expensive OECD country in this market. Despite a more dynamic mobile market prices are high here too, reflecting the relative lack of competition and high unmet demand.

Table 14. **TPSA's profit statement**

	1997	1998	1999	2000	CAGR (%)
Revenues (PLN million)	8 924	10 887	13 160	14 685	10.5
Operating expenses (PLN million)	6 460	8 603	10 320	11 528	12.3
Total investment (PLN million)	4 251	4 071	5 709	6 225	7.9
Operating profit (PLN million)	2 484	2 284	2 840	3 157	4.9
Net profit (PLN million)	N.A.	774	1 029	2 178	
Number of lines in service (PLN thousand)	7 465*	8 514	9 643	10 233	

* Total fixed access lines in Poland times TPSA's market share from Table 2.
Source: TPSA Annual Report 1999 and Unconsolidated Quarterly Report SA-Q IV/2000 Form, January 2001.

Figure 2. **OECD Composite Residential basket**
November 2001, VAT included, USD PPP



Note: Excludes calls to mobiles.

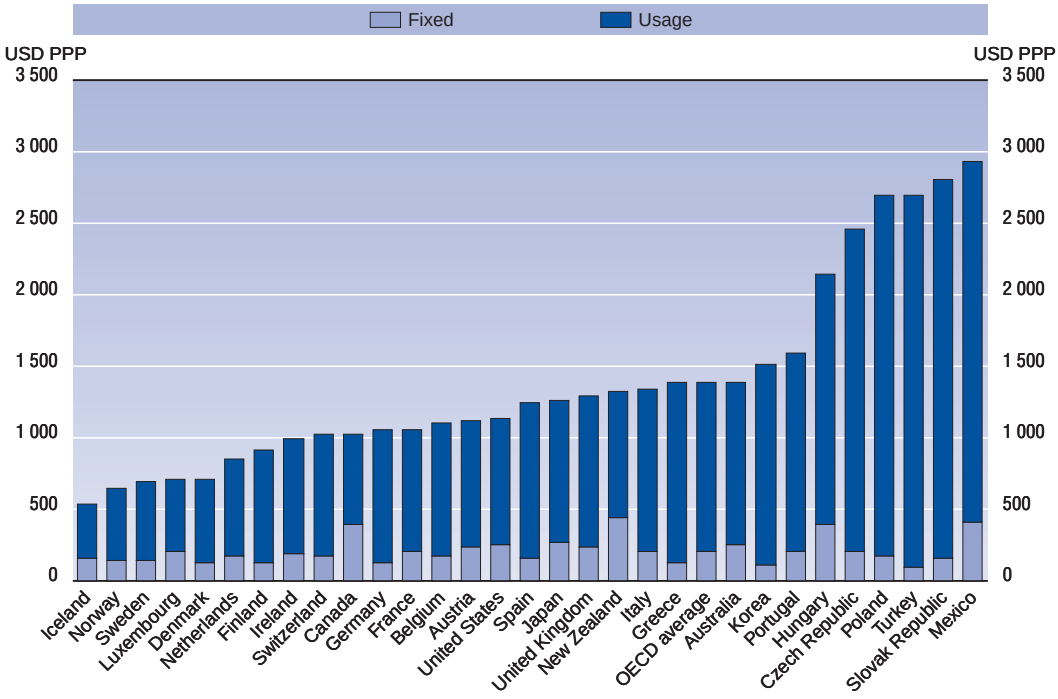
The use of *leased lines* is essential for new entrants to develop their own services, and for Internet Service Providers (ISPs) to deliver broadband access for Internet. Prices are slightly above the OECD average for low speed circuits, but expensive for high speed circuits.

Quality of service has improved (in terms of faults per line and repair times),but still has some way to go. This is linked to investment and technology upgrades, notably digitalisation.

The Polish *Internet* dates back to 1991. TPSA dominates access. This domination is set to continue if regulation is not adjusted to help competitors. There is, for example, no specific interconnection framework between TPSA and ISPs, which are treated as ordinary customers. Even so there are around 300 ISPs, and their numbers are growing. Internet penetration rates are linked to PC penetration and the cost of access. Poland's PC penetration rate was 15.5 per 100 people at the end of 2000, compared with an Internet penetration rate of 13% – the latter could be higher given PC penetration. High access costs are the likely reason for this. The government assesses that Poland is a year behind the least developed EU country in Internet penetration. There is a need to address high access costs, poor infrastructure (though digitalisation and ADSL have increased) and the continued domination of TPSA.

TPSA ranked the lowest among major OECD incumbents in 1999 in terms of *productivity* measured by lines per employee. The poor performance can be accounted for

Figure 3. **OECD Composite Business basket**
November 2001, VAT excluded, USD PPP



Note: Excludes calls to mobiles.

by the requirement to continue network expansion, the lack of competition to encourage greater efficiency, and the presence of a strong union. The TPSA share sale to France Telecom requires that the latter should not impose significant layoffs for a specified period. However restructuring and employment issues are being pursued.

Conclusion

The telecommunications sector in most OECD countries has seen a significant liberalisation and reform over recent years. By 2001, 27 OECD countries had unrestricted market access to all forms of telecommunications, including voice telephony, infrastructure investment and foreign investment. These countries have recognised that the telecommunications sector makes a massive and essential contribution to a modern economy and that infrastructure investment is needed to underpin this. Poland lags these developments by an important margin. The original monopoly incumbent is still hugely dominant in fixed line services, there is still relatively little effective competition, and nearly all the measures of performance (the main exception being mobile services) show a big gap compared with most other OECD countries. Poland seems to have missed the window of opportunity afforded by a relatively late start to draw on experiences elsewhere to promote competition fast and well.

The 2000 Telecommunications Law is driven largely by the need to transpose EU law for accession. It lays a broad legal foundation for fuller liberalisation, including the establishment of an independent regulator (but one with inadequate powers). But it

contains a number of important flaws, omissions and ambiguities (for example in relation to interconnection and universal service). Better consultation in the drafting process would have helped to ensure a better product. The Law's provisions need to be given effect urgently by secondary legislation, a challenge given the Ministry's much reduced staff. However work is proceeding. The handling of TPSA's second share sale does not inspire confidence that the government has yet fully embraced the importance of effective competition to bring Poland's telecommunications services up to scratch. There is a need to acknowledge this and take the necessary action, quickly, to consolidate a regulatory framework which will promote a fully competitive market.

1. Recommendations

1. Accelerate full competition in the telecommunications market: remove remaining monopolistic privileges

The original monopoly incumbent, TPSA, continues to dominate the fixed line telephony market. Under current government policy it will continue to have a monopoly of international telephone services until 2003. This monopoly keeps TPSA much too strong, and will delay the development of effective competition throughout the market. It gives TPSA the opportunity – denied its competitors – to raise revenues in an unregulated market with high margins, and raises the danger that its local services will be cross-subsidised.

The 2000 Telecommunications Law nevertheless provides for TPSA's monopoly to be lifted. Although this may break the agreement with TPSA's strategic privatisation partner (to delay competition), no financial penalty appears to be involved, and the move is essential for the development of competition.

- Take immediate action to abolish TPSA's monopoly on international telecommunications services.

2. Strengthen the competitive framework: adopt strong, fair and cost-based regulation for interconnection charges

Successful competition in a telecommunications market hinges on effective interconnection arrangements. Current regulation has not proved very effective or robust. The Telecommunications Law sets out the procedure for cases where interconnection agreements cannot be concluded. Either of the negotiating parties may apply to the URT for a decision laying down the terms and conditions of interconnection. AURT is a substitute for an agreement. However competitors have experienced difficulties and delays in reaching interconnection agreements with TPSA. It is questionable whether operators' interconnection charges do reflect actual costs, and whether the URT has the expertise to check this. Despite recent improvements, many problems remain.

- Implement, as soon as possible, a new regulatory framework for interconnection.
  - Develop and adopt a calculation methodology based on international best practice – Long Run Average Incremental Cost (LRAIC). In the interim use best practice benchmarks.
  - Base interconnection on call termination, irrespective of whether the networks used are local, long-distance or international.

- Increase the powers of the URT: the Ministry should set principles for interconnection charges and the URT should be responsible for the details
- Specify as soon as possible the methodology for dominant carriers to use in separating their accounts.

3. *Strengthen the competitive framework: tighten up regulation of prices for services of dominant and significant operators*

Price regulation under the provisions of the Telecommunications Law contains good principles but these need to be developed and applied. The Ministry, not the URT, has the main responsibilities. The regulatory framework falls short of what is needed to restrain anti-competitive behaviour by companies who are dominant or have market power.

- Remove exemptions that impede effective price regulation of services offered by companies with a dominant position or significant market power.
  - In particular, eliminate the provision in Article 151 of the 2000 Law that restricts the application of cost-based universal service charges by operators retaining significant market power until 2004.
  - Give the URT powers to devise *ex ante* regulation to protect new entrants against price discrimination.

4. *Strengthen the competitive framework: implement number portability*

Number portability (keeping the same number when switching supplier) also needs to be regulated to ensure a level playing field for competing suppliers. Yet the 2000 Law has no specific provision, apart from noting the possibility of including number portability in interconnection agreements.

- Amend the 2000 Law to ensure that customers switching supplier may keep their number, subject to technical feasibility.
- Require TPSA to offer portability as soon as it is technically feasible. Give TPSA a clear schedule for investment in digitisation.
- Give the URT authority to implement portability.

5. *Promote effective universal service: introduce a regulatory framework based on best international practice*

Poland has a very low level of telephone penetration and the current regulatory framework does not provide adequate incentives for developing universal services. The funding mechanism also needs attention.

- Introduce a new framework for provision of universal service, by setting up a universal service fund and/or by designating TPSA as universal service provider
- Subject TPSA to clear investment targets for network roll-out in rural areas for so long as it remains the dominant operator. Incorporate the targets into the new universal service framework when it is in place.

6. Strengthen the competitive framework: implement asymmetric regulation and match obligations to market power

Although the 2000 Law recognises that regulation will be asymmetric depending on market power in such markets as interconnection and leased lines, it applies this principle inconsistently. New entrants and operators without significant market power are often subject to the same rules and obligations as operators with significant market power. For example, all fixed line public operators must provide connections to all customers on request, a provision that may deter new entrants and distort their investment decisions.

Also, no distinction is made between TPSA and the other operators, despite the fact that it still accounted for over 93% of the local telephony market in 2000, that it shares the long distance market with just three others and that it retains a monopoly of international services. The whole framework of regulation needs to be reviewed to ensure that an appropriate asymmetric approach is implemented, which distinguishes clearly between TPSA, the other operators which are dominant or with significant market power, and the rest.

- Review the current regulatory framework and implement asymmetric regulation.
  - Remove the universal service obligations on new entrants and operators without significant market power (apart from appropriate payment into a universal service fund if set up).
  - Review whether the interconnection charges of the dominant and significant fixed and mobile operators meet cost-based requirements.
  - Enable new entrants and smaller operators with insignificant market power to determine their tariffs flexibly and remove the obligations imposed on them (concerning the use of transparent and objective criteria).

7. Simplify market entry: replace individual licensing with a general authorisation (class licence) framework and permits

Despite changes under the 2000 Law, including a change in terminology, market entry remains essentially based on the discretionary award of individual licences. The attachment of conditions to these licences by the URT is also discretionary and opaque. The Minister can also adjust the content of authorisations, which undermines the URT's independence of action, and its ability to adjust conditions to market changes.

- Replace the current regime with an authorisation (class licence) regime.
  - Establish class licences for different types of activity, with clear non-discriminatory conditions, under which market entry is open subject only to meeting the conditions relevant to the particular activity.
  - Give the URT power to attach minimal and transparent conditions as necessary.

8. Promote competition in broadband services: implement local loop unbundling for voice and data services

The Law's reference to collocation appears to be interpreted by the government as allowing for some form of unbundling (other than voice), but this is vague and insufficient. The success of Internet high speed broadband telecommunications services depends on unbundled access to the local loop. Given that TPSA is already providing DSL services, it is urgent that new entrants are not placed at a disadvantage.

- Amend the 2000 Law and adopt ordinances to impose explicit and full unbundling obligations, including for voice services, on operators with significant market power.

9. Strengthen the telecommunications regulator and its capacity to promote effective liberalisation in the market: give it powers to initiate regulations

An effective regulator should be able to draft and implement regulations, within the general policy framework set by the government, that are needed to create an efficient and competitive market. The URT's role is limited to enforcing regulations which are determined by the Ministry (albeit in consultation with the URT). This limits its practical independence and does not give it sufficient scope to take flexible regulatory action to meet changing market conditions.

- Ensure a mechanism that allows the regulator to take a leading role and to reflect its view and experiences in drafting ordinances and powers to implement general regulations.
  - Extend its functions to include: supervision of the authorisation process, establishment of *ex ante* conditions for interconnection agreements, establishment of the national numbering plan and the allocation of numbers, setting up accounting separation criteria and the cost accounting system, devising quality of service standards, and determining a framework for universal service including its funding.
  - Ensure that it is effectively staffed and organised for these tasks.

10. Implement the 2000 Telecommunications Law without delay: adopt the ordinances necessary to give effect to the Law

Many of the provisions of the Law depend on the details of ordinances which have to be drafted by the Ministry. Many of these do not yet exist. The Ministry has no clear transparent strategy on timetable and the order of priority for doing this work. A key problem is insufficient staff and resources. Staff were transferred too rapidly to the newly established URT.

- Provide the Ministry of Infrastructure with sufficient skilled staff to put in place rapidly the Ordinances needed to give effect to the 2000 Law.
  - Ensure that a clear and transparent timetable is established for this work.

11. Enhance consultation: make sure it includes all interested parties

Effective consultation helps to ensure effective regulation. There is a legal requirement to consult with the telecommunication industry associations (economic chambers) when enacting Laws or Ordinances. A Telecommunications Council acts as a consultative and advisory body to the URT on matters relating to universal service, network interconnection, frequency management, and compliance with electromagnetic compatibility requirements. A broader consultation framework has recently been provided by the new Freedom of Information Law. Its vigorous enforcement should secure an appropriate dialogue with the society in the future. Had there been better consultation in the past the 2000 Law might have emerged in better shape.

- Make draft policies and regulations from the Ministry and the URT available for comment to *all* interested parties including industry, consumers and labour.
  - Make available the rationale for decisions when they are made.

Annex

Regulatory issue	Policy proposals	Chapter
1. Regulatory quality		
A. PROCESSES		
General quality	• **Continue to enhance general regulatory quality: strengthen processes and criteria for making regulations with a clear timetable**	Regulatory Quality (1)
Quality of new regulations: Regulatory Impact Analysis	• **Implement RIA for all new regulations: establish a clear and comprehensive implementation plan**	Regulatory Quality (3)
	– In implementing RIA for new laws and regulations, specifically integrate international trade and investment issues	Market Openness (3)
Consultation	• **Enhance consultation and communication in the rule-making process**	Regulatory Quality (4)
	– Promote more consultation by the competition authority in developing policy	Competition policy (5)
	– Widen opportunities for consultation with all stakeholders in the rule-making process for trade and investment issues	Market Openness (4)
	– Enhance consultation on telecommunications regulations: make sure it includes all interested parties	Telecomm Sector (11)
Accountability	• **Ensure effective enforcement and compliance with the new openness and accountability standards set up by the Freedom of Information Law**	Regulatory Quality (5)
Transparency, simplification	• **Reduce administrative discretion: improve transparency and simplify forms and procedures**	Regulatory Quality (6)
	– Improve the business environment by streamlining administrative formalities	Market Openness (1)
	– Simplify market entry in telecommunications: replace individual licensing with a general authorisation (class licence) framework and permits	Telecommunications Sector (7)
Implementation, compliance and enforcement	• **Improve implementation of, and compliance with, regulations**	Regulatory Quality (8)
	– Promote effective enforcement of trade and investment regulations	Market Openness (2)

Regulatory issue	Policy proposals	Chapter
B. INSTITUTIONS		
Centre of government	• **Strengthen key central institutions to drive regulatory policy**	Regulatory Quality (2)
Local government	• **Strengthen the regulatory quality of local government**	Regulatory Quality (9)
Courts	• **Reduce delays in courts**	Competition Policy (4)
Competition authority	• **Promote effective independence of the competition authority from political influence**	Competition Policy (1)
	• **Provide sufficient resources for the competition authority to retain staff and perform new functions**	Competition Policy (3)
	• **Ensure close and consistent co-operation between the competition authority and sectoral regulators**	Competition Policy (7)
Sectoral regulators	• **Clarify and develop the framework for independent regulatory agencies**	Regulatory Quality (7)
	– Ensure that the Energy Regulatory Authority can effectively resolve problems of access to the grid	Electricity Sector (5)
	– Strengthen the telecommunications regulator and its capacity to promote effective liberalisation in the market: give it powers to initiate regulations	Telecommunications Sector (9)
C. REREGULATION		
• **Consider a mechanism to fund the delivery of the universal service obligation if competition undermines the profitability of Polish Post**		Postal Sector (3)
• **Pursue the proposed system (SOK) for resolving the problem of long term electricity contracts**		Electricity Sector (2)
• **Rebalance electricity tariffs with a view to completing this before EU accession**		Electricity Sector (4)
• **Take forward gas tariff rebalancing**		Gas Sector (4)
• **Ensure that any future long term gas contracts are justified as essential for security reasons**		Gas Sector (5)
• **Complete the regulatory framework for access to gas transmission, distribution and storage services, opting for regulated access under the authority of the ERA**		Gas Sector (6)
• **Strengthen the competitive framework for telecommunications: adopt strong, fair and cost based regulation for interconnection charges**		Telecomm Sector (2)
• **Strengthen the competitive framework for telecommunications: tighten up regulation of prices for services of dominant and significant operators**		Telecomm Sector (3)
• **Strengthen the competitive framework for telecommunications: implement number portability**		Telecomm Sector (4)
• **Promote effective universal service: introduce a regulatory framework based on best international practice**		Telecomm Sector (5)
• **Strengthen the competitive framework for telecommunications: implement asymmetric regulation and match obligations to market power**		Telecomm Sector (6)
2. Competition Policy		
• **Make state aid control a high policy priority: promote the OCCP's new powers to monitor and control state aids**		Competition Policy (2)
• **Improve merger notification rules: eliminate the market share test**		Competition Policy (6)
• **Resist using the concept of "economic dependence" in a way that stifles competition**		Competition Policy (8)
• **Ensure competition authority vigilance over Polish Post behaviour as the postal market is liberalised**		Postal Sector (4)
• **Ensure competition authority vigilance over the oil refining market**		Oil Sector (3)

Regulatory issue	Policy proposals	Chapter
• **Ensure competition authority vigilance over the oil distribution/retailing market**		Oil Sector (4)
3. Market Openness		
• **Pursue progress in the adoption and use of international standards and mutual recognition agreements**		Market Openness (5)
• **Continue to modernise customs procedures**		Market Openness (6)
• **Maintain a liberal import regime to promote competitive oil supply**		Oil Sector (2)
• **Ensure that coal imports and exports meet competitive criteria and are transparently managed**		Coal Sector (5)
• **Phase out discrimination against electricity imports for access to the grid**		Electricity Sector (6)
• **Liberalise access to transmission for imported gas as soon as possible. Aim to remove import restrictions, and to treat imports and domestic gas the same, from the date of EU accession**		Gas Sector (7)
4. Liberalisation privatisation and structural reform		
• **Accelerate liberalisation of the postal sector: adopt the new Postal Law**		Postal Sector (1)
• **Ensure that Polish Post has robust accounting separation**		Postal Sector (2)
• **Continue the process of corporatising Polish Post**		Postal Sector (5)
• **Complete oil sector privatisation plans as soon as possible, taking care to promote a competitive market structure**		Oil Sector (1)
• **Complete the coal restructuring programme as currently set out**		Coal Sector (1)
• **Assess the sustainability and competitiveness of the resulting coal industry structure**		Coal Sector (2)
• **Pursue privatisation once mines are profitable**		Coal Sector (3)
• **Use state aids to restructure the coal industry: base these on transparent taxes**		Coal Sector (4)
• **Continue with the present electricity privatisation plan, maintaining substantial separation of generation and distribution to preserve competition in these sectors**		Electricity Sector (1)
• **Address the competition constraints arising from the vertically integrated electricity transmission company; establish an independent system operator or unbundle PSE's trading activities from its other activities**		Electricity Sector (3)
• **Proceed with the planned privatisation and restructuring of the gas industry**		Gas Sector (1)
• **Ensure that gas transmission activities are quickly and effectively separated from other activities**		Gas Sector (2)
• **Consider divesting gas storage assets to create competitive market in storage services**		Gas Sector (3)
• **Introduce full competition in the telecommunications market; remove remaining monopolistic privileges**		Telecomm Sector (1)
• **Promote competition in broadband services: implement local loop unbundling for voice and data services**		Telecomm Sector (8)
• **Implement the 2000 Telecommunications Law without delay: adopt the ordinances necessary to give effect to the Law**		Telecomm Sector (10)

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