

Fair Market Conditions for
Competitiveness in the Adriatic Region

The OECD Competition Assessment Toolkit



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Policy Briefing Note

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The OECD Competition Assessment Toolkit provides a general methodology for identifying unnecessary regulatory restraints and developing alternative, less restrictive policies that still achieve government objectives. Governments can use the Toolkit to:

- ✓ Evaluate draft new laws and regulations (for example through regulatory impact assessment programmes).
- ✓ Evaluate existing laws and regulations (either in the economy as a whole, or specific sectors)
- ✓ Evaluate the competitive impacts of regulations (either by the government bodies that develop and review policies – or the competition authority)

The toolkit can be used by officials without specialized economic or competition policy training. Potential users include: ministries, legislators, government leaders' offices, sub-national governments and external policy evaluators.

What is the issue?

Increased competition can improve a country's economic performance, open business opportunities to its citizens and reduce the cost of goods and services throughout the economy. However, numerous laws and regulations restrict competition in the marketplace. Many go further than necessary to achieve their policy objectives.

The OECD's Competition Assessment Toolkit (OECD, 2019) helps governments to eliminate barriers to competition by providing a method for identifying unnecessary restraints on market activities and developing alternative, less restrictive measures that still achieve government policy objectives.

The Toolkit consists of three Volumes which build on each other, i.e. the Toolkit Principles (Volume 1), the Technical Guidance (Volume 2) and the Operational Manual (Volume 3).

Figure 1 Competition Assessment Toolkit



What can policy makers in the Adriatic Region do?

Policy makers in the Adriatic region can refer to The OECD Competition Toolkit (2019) to guide them in their competition assessments as this OECD Toolkit is the most comprehensive guide for competition assessment available today. It can also be applied in a decentralised manner across different levels of government.

Volume 1: Toolkit Principles

This Volume of the Toolkit sets down the Toolkit principles, describing the benefits of competition, the Competition Checklist and its role in the competition assessment process.

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

The Toolkit shows regulators and legislators how to make that assessment. It provides a practical method to identify important competitive restrictions and, if possible, how to avoid them.

As a first step, the method employs a “Competition Checklist”, a set of threshold questions which indicate when proposed law or regulation may have significant potential to harm competition. The Checklist helps policymakers focus on potential competition issues at an early stage in the policy development process. While the majority of regulations do not present a risk of significant harm to competition, the competition assessment process, of which the checklist is the initial stage, provides analytical framework for regulators and legislators to mitigate, or avoid, potential competition problems. It does so by helping to identify possible alternatives that may reduce, or eliminate, potential harm to competition while continuing to achieve the desired policy objectives. The questions in the Competition Checklist are grouped into four categories (see below).

Figure 2 Competition Assessment Checklist

COMPETITION ASSESSMENT CHECKLIST

Competition assessment should be conducted if a legal provision has any of the following effects:

A Limits the number or range of suppliers

This is likely to be the case if the provision:

- A1** Grants exclusive rights for a supplier to provide goods or services
- A2** Establishes a license, permit or authorisation process as a requirement of operation
- A3** Limits the ability of some suppliers to provide a good or service
- A4** Significantly raises cost of entry or exit by a supplier
- A5** Creates a geographical barrier for companies to supply goods, services or labour, or invest capital

B Limits the ability of suppliers to compete

This is likely to be the case if the provision:

- B1** Limits sellers' ability to set prices for goods or services
- B2** Limits freedom of suppliers to advertise or market their goods or services
- B3** Sets standards for product quality that provide an advantage to some suppliers over others, or are above the level that some well-informed customers would choose
- B4** Significantly raises costs of production for some suppliers relative to others (especially by treating incumbents differently from new entrants)

C Reduces the incentive of suppliers to compete

This may be the case if the provision:

- C1** Creates a self-regulatory or co-regulatory regime
- C2** Requires or encourages information on supplier outputs, prices, sales or costs to be published
- C3** Exempts the activity of a particular industry, or group of suppliers, from the operation of general competition law

D Limits the choices and information available to customers

This may be the case if the provision:

- D1** Limits the ability of consumers to decide from whom they purchase
- D2** Reduces mobility of customers between suppliers of goods or services by increasing the explicit or implicit costs of changing suppliers
- D3** Fundamentally changes information required by buyers to shop effectively

Checklist A: Are there limits on the number or range of suppliers?

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

- A1: Grants exclusive rights for a supplier to provide goods or services
- A2: Establishes a license, permit or authorization process as a requirement of operation
- A3: Limits the ability of some suppliers to provide a good or service
- A4: Significantly raises cost of entry or exit by a supplier
- A5: Restricts the geographic flow of goods services, capital and labour

Checklist B: Are there limits on suppliers' ability to compete?

Regulation can affect a supplier's ability to compete in a variety of ways, including: advertising a marketing restrictions; standard setting for products or service quality; and price control of goods or services. These limits can reduce the intensity and dimensions of rivalry, yielding higher prices for consumers and less product variety.

- B1: Controls the prices at which good or services are sold
- B2: Restricts advertising and marketing
- B3: Sets standards for product quality that provide an undue advantage to some suppliers over other , or are above the level that some well-informed customers choose
- B4: Raises the cost for some suppliers relative to others

Checklist C: Are there reductions in the incentives for suppliers to compete?

Regulations can affect supplier behaviour by not only changing their ability to compete, but also by changing their incentive to act as vigorous rivals. The main reasons suppliers may compete less vigorously are due to regulations that: may facilitate co-ordination between them or reduce the willingness, ability or incentive of customers to switch between different suppliers.

Other reasons include profit or market share limits that restrict potential rewards from competing. Cartel-like behaviour may be more readily generated under self-regulatory or co-regulatory regimes, by increasing the share of supplier output and price information, or by excluding an industry or sector from the reach of competition law.

- C1: Self-regulation and co-regulation
- C2: Requirements to publish information on supplier prices, outputs or sales
- C3: Exemptions from general competition laws

Checklist D: Are there limits on choices and information available to consumers?

- D1: Limits the ability of consumers to decide from whom they purchase goods or services
- D2: Reduces the mobility of customers by increasing the costs of changing suppliers
- D3: Fundamentally changes information required by buyers to shop effectively

When the answer is “yes”

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

Checklist users will most likely find that only a minority of regulations have the potential to unduly constrain market activity. But when the Checklist suggest that there is a potentially excessive constraint on market activity, a more comprehensive competition assessment merits consideration.

Competition assessment is the process of evaluating government regulations, rules and/ or laws to 1) identify that may unnecessarily impede competition and 2) redesign identified regulations so that competition is not unduly inhibited. Volume 1 of the Toolkit gives a detailed analysis how competition assessment can be affectively incorporated into government activities. To sum it up, fitting this process effectively into government operations and institutions requires consideration of the following five questions:

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

Incorporating competition assessment into government regulatory decision making can potentially yield strong economic benefits. It enables identification of markets where activity is unduly restricted and can propose policy alternatives that will continue to meet policy goals while promoting competition to the extent possible. The best way to fit competition assessment into government operations will vary, given the substantial difference in institutional, legal, federal environments of jurisdictions. Nevertheless, the following points are evident:

- First, regulatory gatekeepers are well-suited to perform competition assessments
- Second, competition authorities are ideally suited to advise on, and even selectively perform, competition assessments and provide training on the process;

- Third, the benefits accrued from fitting an effective competition assessment programme into government regulatory operations definitely outweigh the costs (OECD, 2019).

Volume 2: Technical Guidance

Volume 2 of the Toolkit provides detailed technical guidance on key issues to consider when performing a competition assessment. The central objective of this Volume of the Toolkit is thus to provide a framework for assessing the impact of various rules and regulations imposed by governments and professional organisations on the extent of competition in markets.

Governments often intervene in markets to regulate their structure, or the behaviour of businesses.

Economic interventions can include:

- ✓ Restrictions on starting or expanding businesses;
- ✓ Regulations that affect actions that companies take to compete with each other;
- ✓ Regulations that restrict the incentives of companies to compete; and
- ✓ Regulations that limit the choice or information available to consumers.

Consequences of such interventions can have significant impacts on the affected sectors and, at times, reduce productivity and harm consumers. Volume 2 of the Toolkit explains how to identify whether an intervention may be unduly harmful and provides examples of the development of alternatives.

First, Chapter 1 of Volume 2 explores the need for regulation and regulatory reform. There can be good economic reasons for such interventions, such as preventing market failures arising from the presence of externalities, overseeing common public resources and public goods, limiting market power, and reducing inefficiencies from insufficient or asymmetric information. In addition to economic regulation, governments regulate businesses' behaviour to promote valuable goals in areas such as health, safety and environmental quality.

Then, Chapter 2 of Volume 2 briefly discusses the OECD's initiatives in regulatory reform and the role that competition assessments might play in improving regulation quality.

Finally, Chapter 3 Volume 2 presents key concepts used by competition authorities in their conduct of competition law enforcement. The concepts relate to market power, structure of markets, barriers-to-entry, entry and exit of firms, efficiency and innovation, and the behaviour of incumbent firms, among others. The primary objective here is to familiarise officials conducting competition assessments with key concepts that can be used to evaluate the harm to competition that may be caused by various rules and regulations.

Volume 3: Operational Manual

This Volume 3 of the Toolkit is an *Operational Manual*, which provides a step-by-step process for performing competition assessment. It shows how to assess laws, regulations and policies for their competition effects, and how to revise regulations or policies to make them more pro-competitive. The process can yield substantial benefits to consumers and can significantly increase productivity.

Accordingly, the assessor can develop pro-competitive regulations by:

1. Identifying restrictions to competition.
2. Developing policy options.
3. Comparing policy options.
4. Recommending one or more preferred options.

Many governments have already engaged in competition assessment exercises. Volume 3 of the Toolkit seeks to bring together these experiences into a practical approach for completing competition assessments, with illustrative examples. The approach is well-suited either to ex-ante reviews of new regulations or ex-post reviews of existing ones. One key lesson from reform experiences is that stopping anti-competitive regulation at the draft stage is much easier than advocating change to the regulation after it has entered into force. To have an effective regime of competition assessment, regulations should be reviewed for anti-competitive effects before the regulation enters into force.

Competition assessment is most effective when those people doing it (the assessors) have a clear understanding of the government policy objectives that need to be met, knowledge of technically feasible means for achieving these objectives, sufficient information for comparing options, sufficient resources for conducting an analysis, and sufficient technical skills for performing the analysis. Competition authority staff may be well placed for this type of work; other bodies of government may also have staff with the necessary skills.

Different types of competition assessment

Competition assessment can be performed in a wide variety of situations where government policy interventions are occurring. Assessors can focus on new regulations or pre-existing regulations. Assessors can focus broadly on entire sectors or more narrowly on a particular product market that does not function well.

1. Review of new regulation

When a new regulation is developed or introduced, many countries review the new regulation for its competitive effects. This process is called regulatory impact analysis (RIA). The RIA process can include an explicit competition element. Sometimes existing regulation has sunset clauses that require review before the regulation can be re-enacted. Such sunset clauses are also good opportunities to review regulations for their competitive effects.

2. Focused market study

A market study takes a market where competition does not appear to work well and examines whether the market really has a competition problem and, if so, the likely origins of the problem, and possible policies for reducing or eliminating the problem.

3. Sectoral review

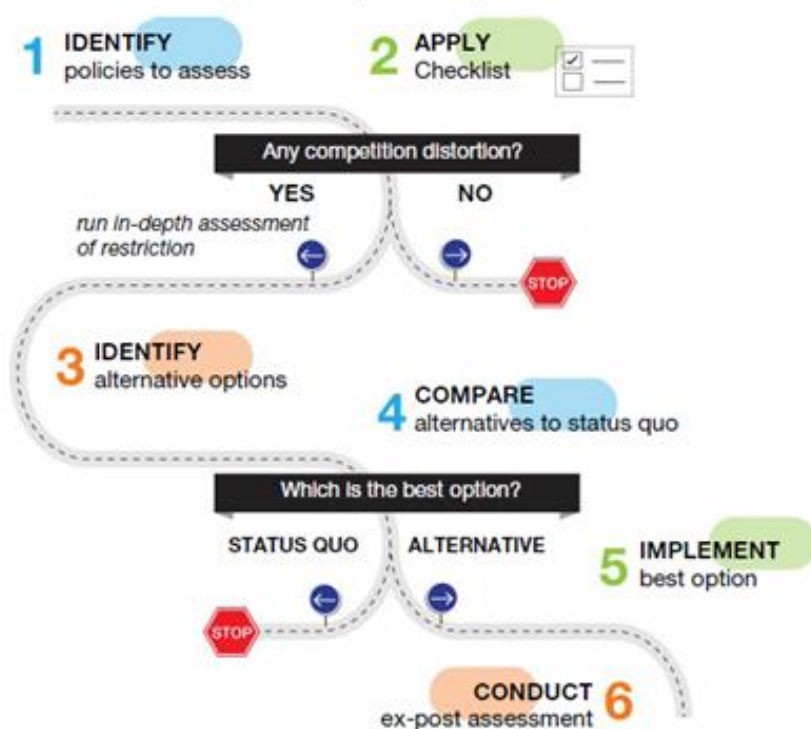
In a sector review, the regulations relevant for a sector are systematically identified and then considered one by one for any restrictions on competition. Like a market study, sector reviews are a form of ex-post analysis as opposed to an ex-ante review conducted by a RIA exercise. Sector reviews do not start with a general presumption that competition is not working in the sector, but instead begin with a search for individual regulations that may unduly restrict competition. Sector reviews may be carried out by the ministry responsible for the sector, though at times such ministries may be committed to existing regulations and-or may not have the necessary expertise in competition assessment. Another alternative for sector reviews is that they be completed by outside entities, such as other bodies of government, like a competition authority, or outside experts.

Process

The process of competition assessment is built around 6 steps (Figure 1).

- ✓ **Step 1.** Identify policies to assess. Identifying the policies to assess can be straightforward (in the case of a review of new legislation or regulations) or complex, as in the case of a sector review, or potentially a market study.
- ✓ **Step 2.** Apply the Checklist. The Competition Checklist (“Checklist”) is a set of four lead questions, each with sub-questions that identify regulations with the potential to restrict competition. ‘Yes’ answers to the questions suggest a need for more detailed analysis of competitive effects of the regulations.
- ✓ **Step 3.** Identify alternative options. When a restrictive regulation is found, it may be possible to identify alternative less restrictive measures that can be used to achieve the relevant policy objectives based on an understanding of the rationale for the regulation, the broader regulatory environment and the technical features of the sector being regulated. This is explored in Chapter 5.
- ✓ **Step 4.** Select best option. Between the options that are identified, the reviewer of the competitive impacts of the regulation must make a judgment about what is (are) the best option(s) – see Chapter 6. There may be more than one best option. Differences between the preferred option and currently proposed or existing regulations must be clearly explained.
- ✓ **Step 5.** Implement best option. Once the best option is identified, appropriate legislation must be drafted and recommendations made to the competent authority. (Chapter 7).
- ✓ **Step 6.** Review impact. Once an option has been implemented, particularly if it restricts competition, it is important to review its impacts (Chapter 8).

Figure 3 Steps in Competition Assessment



A wide-ranging review can produce long-term results

Many regulatory changes may look small, involving sectors that do not account for a large share of GDP. Yet the accumulated weight of unnecessary and unduly harmful regulation across many sectors is a major burden on productivity. When a government identifies and revises a host of policies that unduly limit competition, the aggregate effect can be very large. For this reason, a competition assessment process should not focus exclusively on “large” sectors, but also look at “small” ones across the economy. Dramatic improvements in productivity cannot be expected to appear instantly. After the regulatory environment is improved, changing productive processes can still take time. However, over a period of years, a consistent process of competition assessment can raise productivity and living standards.

Where do we go from here?

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

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

Feedback from Adriatic countries' experiences vis-à-vis the toolkit could ensure that it continues to evolve in line with market developments and users' needs and expectations.

Sources

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The Competition Assessment Toolkit (Brochure) can be consulted at:

<https://www.oecd.org/daf/competition/42228385.pdf>



POLICY BRIEFING NOTES
**FAIR MARKET CONDITIONS FOR COMPETITIVENESS
IN THE ADRIATIC REGION PROJECT**

High levels of corruption and lack of transparency are key constraints to economic growth and competitiveness in many countries worldwide. The Policy Briefing Notes, designed for stakeholders from the Adriatic Region, aim to provide practical guidance to tackle corruption, foster integrity and level the playing field for all firms. They draw on OECD guidelines, legal instruments and good practices and are tailored to the region's circumstances.

The Policy Briefing Notes are one output of the three-year OECD project to promote fair market conditions for competitiveness in Bosnia and Herzegovina, Croatia, and Serbia, supported by the Siemens Integrity Initiative. Through Collective Action, government officials from the region along business leaders, anti-corruption experts and practitioners, civil society representatives and academics have engaged to jointly identify country-specific challenges to integrity and foster fair market competition.

These efforts are part of the engagement of the OECD South East Europe Regional Programme, which collaborates with the region since 2000 to foster private sector development and competitiveness, improve the investment climate and raise living standards for an inclusive and sustainable future for the people of South East Europe.

**www.oecd.org/south-east-europe
oe.cd/fair-market-conditions**