COMPETITION AUTHORITY OF KENYA

Creating efficient markets for consumers

ASSESSMENT OF REGULATORY IMPACT ON COMPETITION

Guidance For Policy Makers

economy discrimination alternatives consultation consumer choice
restrictions to entry policy makers market failures barriers information
discrimination markets pro-competitive regulations policy objective trading
pro-competitive solutions anti-competitive prices impact

ASSESSMENT OF REGULATORY IMPACT ON COMPETITION

Guidance for Policy Makers

November, 2015

TABLE OF CONTENTS

FIGURE

LIST OF BOXES

ACKNOWLEDGMENTS

This guideline was developed as part of the cooperation agreement between the IFC, a member of the World Bank Group, and the Competition Authority of Kenya (CAK). Activities were carried out under the Kenya Investment Climate Program, implemented by the Trade and Competitiveness Global Practice of the World Bank Group, in partnership with the United Kingdom Department for International Development (DFID) and the Dutch Government.

The Advocacy and Research Department of CAK headed by Lilian Mukoronia (Manager, Advocacy) was responsible for the preparation of the guidelines. Tania Begazo (Senior Economist and Competition Specialist) led the World Bank Group's Trade and Competitiveness team that supported the development of this guideline: Philana Mugyenyi (Competition Analyst) and Sara Nyman (Economist). This guideline also benefitted from valuable technical guidance by Martha Martinez Licetti(Senior Economist, Global Competition Policy Team Lead, Trade and Competitiveness, World Bank Group).

The CAK gratefully acknowledge the inputs provided by various government counterparts that participated in the validation workshop held in Nairobi on March 17, 2015 and institutions that provided written comments on the draft guidelines including the Central Bank of Kenya.

PART 1

PURPOSE AND SCOPE OF THIS GUIDELINE

BACKGROUND

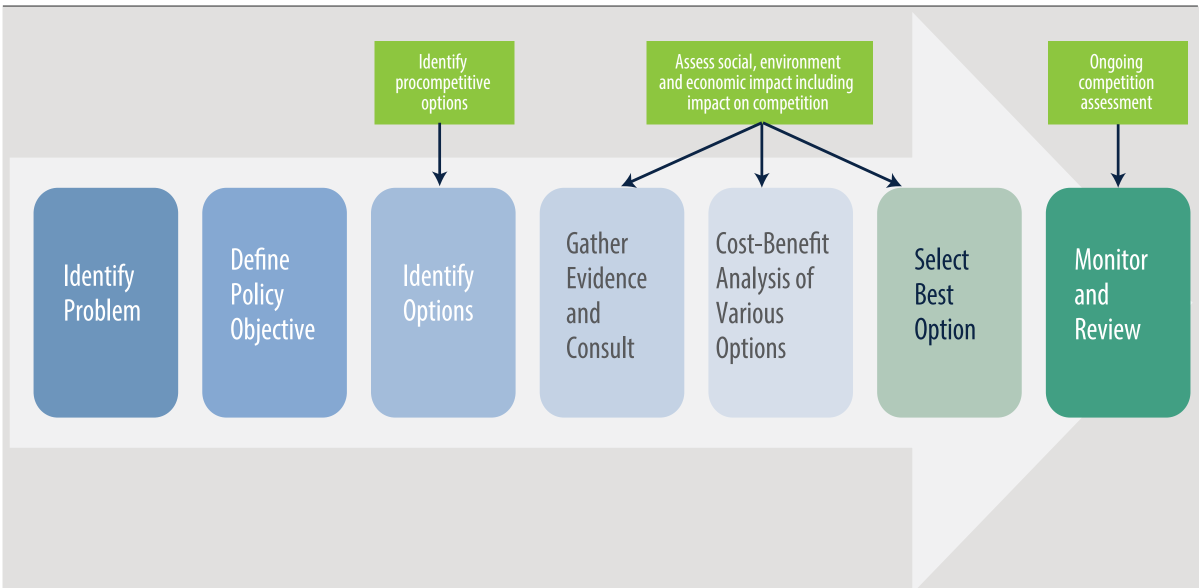
Assessing the impact of regulation

In order to ensure policy objectives are achieved in the most effective manner, policy makers consider the costs and benefits (or impact) of proposed policies, bills and regulations. In Kenya, the Statutory Instruments Act, 2013, requires regulatory authorities to prepare a regulatory impact statement for every statutory instrument (rule, order, regulation, form, by-law, resolution, etc.) that is likely to impose significant costs on the community. As per the Act's schedule, the statement shall include an analysis of the impact on the private sector. The impact on the private sector includes, among other things, the effects on competition conditions. Furthermore, the Act requires public consultation of all the statutory instruments that have an effect on competition. Figure 1 below illustrates how an assessment of a regulation's impact on competition can be incorporated into regulatory impact assessments, following the practice of other jurisdictions such as Australia, European Union (EU), Mexico, and United Kingdom (UK).

Some policies, laws, and statutory instruments which are intended to meet public policy objectives can also reduce the level of competition in markets by:

- Making it more difficult for new competitors to enter the market, by creating undue regulatory requirements that are difficult and costly for them to meet;

Figure 1: The regulatory impact assessment process and how to incorporate competition assessments



Source: WBG.

- Preventing firms from competing strongly or reducing their incentive to do so – for example, by setting rules that reduce price competition or restrict advertising;
- Distorting the level playing field and preventing firms from competing on their merits, by allowing for broad discretion in the application of regulations or establishing regulations that favour certain firms;
- Increasing the costs for consumers to switch to more competitive providers, by reducing their mobility or the amount of information available to them.

This reduction in competition is a particularly important cost affecting the private sector, consumers, and the economy as a whole. It is therefore important to objectively justify the costs of such restrictions on competition relative to the benefits, or to seek a less costly alternative.

The Role of the Competition Authority of Kenya in enhancing regulatory design

The Competition Authority of Kenya (CAK) is a State Corporation established by Section 7 of the Competition Act No.12 of 2010. The CAK is mandated to promote and safeguard competition in the national economy and protect consumers from unfair and misleading market conduct. As such, in line with sections 5 and 9 of the Competition Act, the CAK has a role in studying government policies, procedures, programmes, legislation and proposals for legislation so as to assess their effects on competition and consumer welfare and provide its opinion.

OBJECTIVE OF THIS GUIDELINE

The objective of the Guideline and Checklist is to provide a general approach for policy-makers in Kenya to screen for and identify the impact of laws and regulations with the potential to restrict competition; and also assist in developing alternative, less restrictive policies that will achieve government policy goals. Policy makers may use the guideline to evaluate both existing and draft laws and regulations[1].

The CAK is willing to provide assistance to policy makers who are responsible for the introduction of new regulations—especially those that are expected to have an impact on businesses—at any stage in the policy development process, but recommends that advice is sought at an early stage. Policy makers can consult the CAK where they are uncertain as to whether a proposed policy or regulation may affect competition in the markets. A positive answer to any of the questions included in the checklist would trigger consultation with CAK; however, government officials are encouraged to request CAK's advice in other situations that could lead to negative effects on competition.

This Checklist and Guideline provide guidance for policymakers on how to apply a screening test to assess whether a proposed (or existing) regulation is likely to result in major anti-competitive effects.

The Checklist and Guideline:

- Provides a checklist of the four main ways that a proposed regulation could restrict competition in markets and those provisions with higher risk of harming competition (chapter 2).

[1] The term 'regulation' and 'statutory instrument' will be used interchangeably and encompass rules, orders, regulations, forms, by-laws, and resolutions.

- Provides broad guidance to policy makers in identifying affected markets (chapter 3)
- Explains why policies that restrict the number or range of suppliers might raise competition concerns and provides examples (chapter 4)
- Explains why policies that restrict or limit the incentives and ability of suppliers to compete vigorously might raise competition concerns and provides examples (chapter 5)
- Explains why polices that discriminate against certain agents might raise competition concerns and provides examples (chapter 6)
- Explains why policies that restrict choice or information available to consumers might raise competition concerns and provides examples (chapter 7)
- Provides guidance on elements for developing pro-competitive solutions to achieve policy objectives (chapter 8).

The examples provided primarily illustrate cases where governments have imposed regulations which harm competition. However, a number of examples show cases in which procompetitive regulatory solutions have been adopted to address non-regulatory risks to competition present in a market (See Boxes 20, 21, 23, 24 and 26).

PART 2

THE COMPETITION CHECKLIST: A SCREENING TEST FOR POLICY-MAKERS

The "Competition Checklist" provided in these Guidelines is designed to function as a screening test for the impact of policies, bills or statutory instruments on competition (Box 1). A screening test allows policy makers to determine whether a proposed policy, bill, or statutory instrument may have significant impact on competition. Policy-makers can complete a screening test based on their knowledge regarding the objective and potential effects of the draft policy, bill, or statutory instrument. For most regulations, the screening test will be sufficient to show that no major anti-competitive impacts are likely. However, if the screening test identifies a risk that there may be a major negative impact on competition, policy makers are encouraged to seek the specialist assistance of the CAK to complete a more detailed assessment.

This Checklist is based on the World Bank Group Checklist on Anticompetitive Regulations, which provides a guiding framework of questions to identify regulations or policies which have a detrimental impact on competition in affected markets. This framework has been developed through the World Bank Group's experience in several countries, and builds on competition assessment frameworks applied by governments internationally, including the UK, the EU, Australia, and Mexico.[2]

2 See for example, Office of Fair Trading, Completing competition assessments in Impact Assessments, Guideline for policy makers, August 2007; Commonwealth of Australia, Department of the Prime Minister and Cabinet, The Australian Government Guide to Regulation, 2014; European Commission, Better Regulation: A Guide to Competition Screening, 2005; COFEMER, Agreement that modifies the manual on regulatory impact and includes the competition analysis, 2012.

The Checklist is based on four simple questions, which ask about the impact of the proposal on the number of firms in the market, their ability and incentives to compete, the level playing field, and the impact of the proposal on choice or information available to market players. These are the major factors influencing the intensity of competition in a market. Under each of the four questions there is a list of commonly-found regulatory or policy restrictions that would have an anti-competitive impact. Certain features of the major factors influencing the intensity of competition generate a higher risk of restricting competition, such as granting monopoly rights and limiting the number of competitors in the market; facilitating collusive conduct by market players and excluding companies and sectors from competition law enforcement; discriminating between competitors regarding legal requirements, fiscal and non-fiscal incentives and access to essential resources; and eliminating the possibility for consumers to switch suppliers. All these areas are highlighted in blue in Box 1.

When applying this Checklist, policymakers are encouraged to bear in mind that all markets are composed of suppliers and buyers and that market power can arise amongst either one of these groups. Therefore, while it is most common to think of harmful anticompetitive effects as a result of market power amongst suppliers, policymakers should take into account that anticompetitive impacts can also arise from the creation of market power amongst buyers. Restrictions which reduce competition between buyers are particularly important in agricultural markets where there are often a large number of scattered small suppliers (or smallholder farmers) facing a small group of concentrated buyers or, in some cases, a single buyer. For example, high buyer power relative to the market power of individual suppliers could depress prices received by farmers for their produce to below the competitive levels. Therefore, when conducting the screening test, it is important for policy makers to consider the impact on both the supplier and buyer sides of the market.

It is also worth stressing that the Checklist presented here provides an initial screening test to identify only whether the regulation in question has the potential to restrict competition. It is acknowledged that a number of other factors will play a role in determining whether ultimately the restriction does in fact unnecessarily restrict competition or whether the net cost of the restriction outweighs the benefit. Such factors might include structural differences between sectors, specific market conditions, or other regulatory objectives in the sector under consideration. These factors would be incorporated into the more detailed competition assessment conducted following the initial screening test.

Furthermore, the fact that a proposed regulation or policy has a major anti-competitive impact does not necessarily mean that it is ill-conceived. However, if a negative effect on competition is identified, other alternatives that are less-restrictive on competition should be considered. Further, it is important to weigh the costs of the restriction on competition against the benefits that the regulation is trying to achieve.

Finally, it is worth noting that the checklist can also be applied to examine the degree to which existing regulations restrict competition. The checklist could be used as part of an enquiry launched by the CAK to analyse competition in a specific market, or as an element of studies carried out by government entities to assess the effectiveness of a regulatory framework in achieving its policy goals.

Box 1: The competition checklist for policy makers

In any affected market (see chapter 3 for definition), would the proposal …	YES	NO
1. Directly or indirectly restrict the number or range of suppliers or buyers? (chapter 4)		
This is likely to be the case if the proposal:		
▪ Awards exclusive rights to a supplier/buyer		
▪ Introduces procurement from a single supplier or restricted group of suppliers		
▪ Introduces a fixed limit on the number of firms (quotas)		
▪ Creates geographical barriers on the ability of companies to supply or buy goods or services		
▪ Establishes licenses, permit or authorisation processes as a requirement for operation		
▪ Limits the ability of some types of suppliers to provide a good or service or the ability of some types of buyers to purchase goods or services		
▪ Creates higher costs of entry or exit for firms		
2. Restrict the ability or incentives of suppliers or buyers to compete vigorously? (chapter 5)		
This is likely to be the case if the proposal:		
▪ Limits the extent to which prices for goods or services are defined by market forces		
▪ Increases scope for self-regulatory or co-regulatory regimes which negatively affect entry conditions, the ability of firms to set prices individually or other market variables		
▪ Introduces requirements that information on firms' outputs, prices, sales, purchases or costs be published or exchanged among competitors		
▪ Exempts the activity of a particular industry or group of firms from the operation of the competition law		
▪ Limits the freedom of firms to advertise or market their goods or services		
▪ Sets standards for product quality that are above the level that some well-informed customers would choose*		
▪ Limits the scope for innovation to i) introduce new products; ii) supply existing products in new ways (using different marketing channels or different sales formats, for example); or iii) purchase products in new ways (using different procurement channels, for example)		
3. Discriminate (or facilitate discrimination) against certain agents? (chapter 6)		
This is likely to be the case if the proposal:		
▪ Introduces discriminatory application of rules against certain types of firms (entrants, foreigners, small firms, private firms) or sets standards for product quality that provide an advantage to some firms over others		
▪ Allows for discretionary application of rules to market players (lack of objective requirements or criteria, reduced accountability)		
▪ Introduces subsidies, incentives policies, and access to limited resources (e.g. land, water, spectrum) that distort the level playing field		
▪ Allows regulators to provide goods or services in competition with private players		
▪ Does not provide for a clear and effective access policy (e.g., non-discrimination, clear conditions, cost-oriented fees) to essential facilities		
4. Restrict the choice or information available to consumers or producers? (chapter 7)		
This is likely to be the case if the proposal:		
▪ Eliminates the possibility for consumers (producers) of switching suppliers (buyers)		
▪ Limits the ability of consumers to decide from whom they purchase		
▪ Limits the ability of producers to decide to whom they sell		
▪ Reduces mobility of consumers between suppliers of goods or services		
▪ Reduces mobility of producers between buyers of goods or services		
▪ Reduces the information available to buyers (producers) to allow them to purchase (sell) effectively		

Criteria highlighted in blue present a higher risk of negatively affecting competition.

PART 3

IDENTIFYING AFFECTED MARKETS

MARKET DEFINITION

A market is commonly understood to consist of both buyers and sellers of a product in a certain geographical area. However, the term "market" has a specific meaning for competition law purposes. The relevant market within which to assess a competition issue has two dimensions: the product market and the geographic market. In most cases, a market consists of a group of similar products (the product market) sold in a particular area (the geographic market).

The CAK generally takes account of the relevant product market and the relevant geographic market in defining the relevant market or markets[3]. The CAK has expertise in defining 'relevant markets' because this is an important step in assessing competition effects. The first and most essential task in market definition is to delineate the product market by identifying all the products that buyers regard as reasonable substitutes for the product under investigation. A relevant product market comprises all those products which are regarded as reasonably interchangeable or substitutable by the consumers, by reason of the products' characteristics, their prices, and their intended use.

[3] The CAK Guidelines on Relevant Market Definition http://www.cak.go.ke/index.php?option=com_docman&task=cat_view&gid=8&Itemid=501

The identification of product market is followed by defining the geographical market, which may extend beyond the area under investigation and in which the product is sold. The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous, and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those areas. Note that markets may be local, regional, national, or international. While policies or regulations may be limited in their jurisdiction, they may have wider effects because of the ability of consumers and suppliers to purchase or supply in a broader geographic area.

AFFECTED MARKETS

When identifying the markets affected by a policy (the "affected markets") it is important to consider:

1. Both directly-affected markets and those which are indirectly affected as a result of consumers or producers switching to alternative products due to the policy change;
2. Whether or not there will be knock-on effects in related markets. The production, distribution, and sale of a product typically occur through a series of functional levels such as manufacturing, wholesale, and retail.

It is often useful to identify the relevant functional level(s) in describing a market, as the proposed policy or regulation may affect one level but not others – or it may affect several functional levels at once. Generally, the policy makers should identify separate relevant (but related) markets at each functional level affected by the proposed policy or regulation being considered, and assess the impact on each.

EVALUATION OF PROPOSED REGULATION

Once the policy maker has identified the markets affected by the proposed policy or regulation, s/he can consider its potential impact on competition by reference to the four questions from the Competition Checklist.

Where there appears to be a significant detrimental effect on competition, the policy maker should consider whether or not there are suitable alternatives to the proposed policy or regulations that limit restrictions on competition while still achieving policy objectives.

ALTERNATIVES TO REGULATION

Where a proposed regulation is likely to adversely affect competition in an affected market, policy makers should consider whether there are alternative proposals that will achieve the same policy objective but with fewer adverse effects. In some cases, market failures can be remedied through semi-regulatory or non-regulatory alternatives, such as:

- Focused incentives (taxes/subsidies)
- Information and education campaigns
- Self-regulation (through trade associations)
- Co-regulation (self-regulation legally recognised, facilitated and enforced by Government).

However, where relevant, the impact of non-regulatory alternatives on competition should also be considered. For example, in the case of self- or co-regulation, it is crucial to design these schemes to ensure that undue discretionary power is not vested in incumbent firms. This will be further discussed in Section 5.v. Incentives should also be designed and awarded in a way that minimises the risk of providing an undue advantage to certain firms or sectors.

Chapter 8 provides guidance on how to identify alternative procompetitive regulatory and non-regulatory measures. In addition, a number of the examples of anticompetitive regulation highlighted in these Guidelines provide illustrations of procompetitive solutions which could be considered as alternatives, or specify where regulators have taken actions to resolve regulatory restrictions to competition.

PART 4

RESTRICTIONS ON THE NUMBER OR RANGE OF SUPPLIERS OR BUYERS

Entry, or the threat of entry, are important factors that exert competitive pressure on existing suppliers. Policies or regulations that directly prevent entry are likely to reduce the competitive pressure faced by existing suppliers (or buyers), with potential adverse effects on prices, quality, and/or range of products or service.

The following scenarios place limits on the number or range of suppliers in affected markets:

i. **Exclusive rights for a supplier to provide goods or services, or procurement of goods and services from a single supplier or restricted group of suppliers.** This scenario results in the establishment of a (private or public) monopoly and acts as the ultimate barrier to entry. Unless there is a justification for such a provision (for instance, in the case of natural monopolies) such restrictions should not be applied in a market. As an example, in Australia, regulations had traditionally granted the Waters and Rivers Commission sole rights to fit, repair, and test water meters. In 2000, the government amended the regulations to remove these exclusive rights, noting that it was harming competition.

   Policy makers considering the introduction of policies that would grant exclusive rights should ensure that the contracts are of relatively short duration to allow for regular competition for the exclusive rights.

   In the case of procurement from single suppliers, policy makers should consider that while there may be clear benefits (resulting from efficiencies in the procurement administration) from awarding a single contract, they should be aware that these benefits should be weighed against the loss of ongoing competition and choice, and expected higher prices.

   Policy makers advising on policies and regulations relating to public procurement can contact the CAK for advice on including pro-competition mechanisms into the design and operation of the proposed policy or regulation. Advice can also be requested for the design of tenders in order to encourage more participation and competition.

ii. **Exclusive rights for a single buyer.** A single buyer is called a *"monopsonist"*. Policies or regulations that restrict the number of buyers in markets with a large number of scattered suppliers create buyer power that can lead to prices below the competitive level, unduly favouring the select buyer(s). This kind of restriction is particularly relevant, for instance, in agriculture markets.

   One example of the restrictions described in i) and ii) is the exclusive rights previously held by the Pyrethrum Board of Kenya (PBK) in the pyrethrum industry. Until the repeal of the Pyrethrum Act of 1964 in 2013, the PBK held monopsony rights to act as the sole purchaser and processor of pyrethrum flowers in Kenya, as well as monopoly rights as the sole marketer of refined pyrethrin extract both domestically and abroad. This situation eliminated choice for farmers and subsequently led to a number of challenges being faced in the Kenyan pyrethrum industry. Under the Crops Act 2013 and the Agriculture Food and Fisheries Act 2013, these exclusive rights have been removed and efforts are underway to open the market to new commercial players to improve the efficiency and competitiveness of the industry. The Agriculture Food and Fisheries Authority (AFFA) will now act as a neutral sector regulator with its regulatory and commercial functions being separated.

iii. **Establishment of a license, permit or authorisation process as a requirement for operation.** This can also cause restrictions on entry of suppliers, particularly if the number of licenses are limited or qualifications requirements are 'too strict' i.e. more than the required minimum to provide the service. Examples of this from the Greek asphalt sector and tourism sector are provided in Box 2 and Box 3. Strict and unnecessary regulations for starting operations result in reduced consumer choice and create artificial scarcity that raises prices. Therefore, a careful balance has to be achieved while formulating such regulations.

Policy makers advising on regulations or policies relating to licensing schemes are advised to contact the CAK for advice on the design and operation of the proposed regime.

Box 2: Overly strict licensing requirements in the Greek asphalt sector create barriers to entry

Anticompetitive Regulation

In Greece, national legislation on oil products provides that in order for a company to obtain a license to trade asphalt:-

1. The minimum share capital must be EUR 500,000.
2. The company should have a minimum storage capacity of 2000m^3 to store the asphalt.

According to recitals of the law, the objective is to ensure the financial capacity and sustainability of the companies trading in oil products, given the high value of the product.

Harm to Competition

These provisions may raise entry costs and constitute a barrier, particularly for smaller suppliers who wish to enter the asphalt market. This is especially true since the lack of definition of land use in a considerable part of the country means that it is difficult to obtain a permit to build a storage tank with such large capacity. As a result, the above provisions may limit the number of suppliers, lead to higher concentration in the relevant market and potentially to higher prices. Additionally, such barriers may enhance the market power of incumbents and lead to anti-competitive behaviour.

Procompetitive Solution

- Abolish the minimum share capital requirements and allow asphalt suppliers to choose the form of company and the share capital they wish to contribute. The value of the product could be safeguarded through insurance contracts rather than through share capital.
- Allow each company to decide its minimum storage capacity according to its financial size and the volume of asphalt it trades.

Source: OECD (2014), OECD Competition Assessment Reviews: Greece, OECD Publishing.
http://dx.doi.org/10.1787/9789264206090-en

Box 3: Strict requirements to obtain permits and licenses in the tourism sector in Greece

Anticompetitive Regulation

Numerous barriers to entry in the tourism sector, many of those resulting from strict requirements to obtain building permits or licenses for certain facilities, such as:

- A Presidential Decree states that car racing tracks must be constructed within a 100km distance of 3,4 or 5-star hotels having a minimum capacity of 1 000 beds and within a 120km distance of airports.
- According to a Joint Ministerial Decision tourist entertainment theme parks may only be established with hotels if these are 3-star or above. A further ministerial decision states that theme parks may only be established in urban areas with a population over 40 000 or within 60km (one hour journey time) of urban areas and communities with a total population of 40 000.
- Centres of athletic and coaching tourism are obliged to operate all year round. A ministerial decision specifies that in periods of low demand such centres should still be able to satisfy the needs of the local population for sports and athletics.
- Brokerage offices must be at least a full 20m^2 and must be exclusively for the use of the brokerage activity. The sharing of office space with other activities is prohibited.

According to the Ministry of Tourism, the objective of these provisions is to protect consumers and tourists, to ensure a high quality of service offered to consumers, to facilitate the viability of the investment and to achieve specific policy goals.

Harm to Competition

Contrary to the stated policy objectives, in practice the requirements may lead to additional and unnecessary significant cost increases, greatly increasing uncertainty for investors and acting as a significant barrier to entry into a specific market.

For instance, the requirement of brokerage offices to have a minimum surface may discourage small investors. This also applies to the requirement for centres of athletic and coaching tourism to operate all year round. The additional costs imposed by the regulation appear significant and are likely to discourage new entrants, especially those without the capacity to operate all year round. Total costs are also increased where the law obliges investors to operate hotel services above 3-star ranking. It may also impose standards above the level at which some well-informed consumers would choose to consume. (See Section 5.iii. for further discussion on this).

Procompetitive Solution

Lifting these barriers to entry would entice more entrants into the market, stimulating competition, thereby leading to improvements in innovation and quality, increasing and the variety of accommodation on offer to tourists. This would make the Greek tourism offer more attractive overall without the need for strict licensing requirements.

Source: OECD (2014), OECD Competition Assessment Reviews: Greece, OECD Publishing.
http://dx.doi.org/10.1787/9789264206090-en

iv. **Limits on the ability of some types of firms to provide (or purchase) a good or service.** Sometimes Governments or professional associations can restrict the ability of some type of suppliers to provide a service. In some cases, policy makers may be persuaded that there is a limit on the number of firms that can operate effectively in an affected market. As a result, policy makers may grant existing suppliers' rights to veto new entry – protecting them from competitive pressure but harming consumers faced with less competition and choice (Section 5.v. discusses this further). For instance, if fee-for-service brokers are not allowed to operate in the real estate market, then only traditional brokers will thrive and customers will be restricted in their choice of real estate brokers and the associated costs of the service.

In the transport sector, cabotage restrictions often restrict the ability of foreign vessels to carry cargo or passengers by sea, air or land within a country, shielding domestic carriers from competitive pressure.

Certain quality standards and certification rules adopted by government or professional organisations also constitute an implicit constraint on entry and impose significant restrictions on competition. Box 4 below provides an example, the case of the Zambian sugar industry.

Box 4: Fortification requirements and administrative trade barriers restrict import competition in the Zambian sugar industry

Anticompetitive Regulation

Zambian legislation requires all sugar meant for direct consumption in the domestic market to be fortified with Vitamin A in specific quantities. The legislation was introduced in 2000 through an initiative of the Ministry of Health.

In addition to the above legislation, there are also administrative barriers to sugar imports including high tariff rates on imported sugar from outside the trading blocs where the country is a member. These rates surpass the rate commonly applied to most finished products (WTO, 2007). In addition, potential importers are required to obtain import permits from the government but the process is not transparent and is often delayed. Imports also have to be cleared by three ministries (Ministry of Agriculture and Livestock, Ministry of Health and Ministry of Commerce, Trade and Industry).

Harm to Competition

Zambia Sugar, the dominant market player, has embraced fortification. However, this legislation does not generally exist in most countries and therefore effectively blocks potential imports from entering Zambia. The requirement therefore effectively limits the influx of cheap imported sugar to the Zambian market – something which had brought Zambia Sugar under pressure before the imposition of fortification requirements, with imports from Malawi and Zimbabwe estimated to have reached 25 percent of Zambia's domestic market pre-fortification (Serlemistos & Fusco, 2010).

The effect of these barriers to trade is evident in the negligible sugar imports of both direct consumption and industrial sugars.

As a result, the market power of millers within Zambia has been entrenched and these players have the ability to price domestic sugar with high margins, raising prices for consumers despite the fact that Zambia is a low-cost sugar producer (Nyberg, 2011). For example, in 2012, Zambia Sugar raised the domestic price of sugar by 14 percent (Lewis, 2013), despite the low costs of production.

Source: Chisanga et al (2014), Competition in the regional sugar sector: the case of Kenya, South Africa, Tanzania and Zambia

v. **A higher cost of entry or exit for firms.** Policy makers should consider whether a proposed policy or regulation will limit the number of firms in the market by significantly raising the costs of entering or exiting the affected market. For example, stringent regulations requiring the clean-up of industrial factories may deter new entrants from leasing such spaces, which might otherwise have been affordable enough to allow new entry. Box 3 also outlines a number of examples of regulations which raise costs for investors in the tourism sector in Greece, such as minimum requirements for hotel rankings at theme parks, obligations for athletic centres to open all year round, and minimum floor space requirements for brokerage firms. Costs of entry and operation can also be through overly short license or permit renewal periods and high renewal fees.

In some cases, the cost of entry might be raised only for specific types of firms. For instance, charging different license fees for foreigners can provide an undue advantage to local suppliers and prevent the entry of foreign firms or individuals. Discrimination between firms is further discussed in Section 6.

vi. **Geographical barriers on the ability of companies to supply or buy goods or services.** These should be assessed on whether there is a clear link between the restrictions and the achievement of specific policy goals. Otherwise, competition will be artificially reduced.

Box 5: Geographic restrictions on retail establishments in Oaxaca, Mexico

Anticompetitive Regulation

Several municipal regulations restrict the entry of companies and investment in retail in the municipality of Oaxaca de Juárez in Mexico. In particular, the number of licenses or positions that can be awarded to an individual agent are restricted, limiting incentives for expansion. Meanwhile, the Commercial Establishments Regulation lays down rules on minimum distances for commercial establishments that sell alcoholic beverages, creating geographic monopolies that limit consumer choice.

One example of the restrictions on minimum distances is the restriction on commercial establishments selling alcoholic beverages. Under the regulations, these must be located more than 100 hundred metres of any school, hospital, church, sports field and establishments with the same or similar line of business. This provision is unclear in scope. While it may have sought to inhibit consumption of the product or eliminate negative externalities generated by the consumption of products in school or sports centres, the limitation goes beyond these objectives by extending the restriction to the location of new establishments “with the same or similar line of business” in the vicinity of other already established businesses, limiting competition.

Harm to Competition

Bans on business establishments within minimum distances from other business often have a negative effect on the consumer by arbitrarily limiting the competition to which providers would otherwise be exposed. The negative impact of such restrictions is greater in those cases where the geographic markets involved are small. Such geographic restrictions should therefore be reviewed to ensure that they are necessary and proportionate to achieve the desired objective.

Source: World Bank (2014), Equipo de Políticas de Competencia, Combatiendo regulaciones que restringen la competencia a nivel sub-nacional: Oaxaca- México

PART 5

RESTRICTIONS ON THE ABILITY OR INCENTIVES OF FIRMS TO COMPETE

Competition between suppliers may focus on price, quality, service, or innovation. Policies or regulations that restrict the means by which suppliers compete with each other can inhibit competition between those suppliers. Such regulations also increase operational risks for businesses.

The following types of regulations usually result in restrictions on the ability of suppliers to compete in the market:

i. **Limits on the extent to which prices for goods or services are defined by market forces.** While regulating prices in traditional monopoly sectors such as utilities might be warranted, price controls in markets where there are many potential suppliers may have adverse effects.

   Minimum prices (or price floors) prevent more efficient low-cost suppliers who could have supplied at a price below the specified minimum from doing so. In the absence of a price floor, consumers would benefit from lower prices, and inefficient producers would have more incentive to find more efficient means of production to remain in the market. If the policy objective of the minimum price was to raise product quality or safety, direct regulation of product quality or safety might be a less restrictive means of delivery.

   Meanwhile, if maximum prices (or price ceilings) are set, incentives to innovate by providing new or high-quality products can be substantially reduced. Maximum prices can also become a focal point for collusion between suppliers with prices drawn to the ceiling, where otherwise a product or service could have been supplied at a lower price. They may also lead to some suppliers exiting the market because of the lower price, distorting the choice of products supplied. Or they could lead to the imposition of hidden charges to circumvent the price ceiling. Price ceilings are often intended to protect consumers from high prices, but there may be less restrictive means of delivering this objective. For example, if high prices were a result of anticompetitive behaviour, it would be more effective to tackle this directly through enforcement of the competition law or to promote competition by lowering entry barriers. Otherwise, demand-side subsidies might also present a less distortive means of protecting consumers from high prices, compared to supply-sideprice controls.

The regulation of marketing margins or the establishment of guidelines or criteria for the setting of tariffs can also impose restrictions on the ability of market forces to determine prices.

In summary, all regulations related to prices must be carefully assessed and consideration should be given to alternative means of meeting policy objectives.

Boxes 7, 8, 9 and 10 provide various examples of the ways in which regulations can distort market prices and place limitations on the ability or incentive of firms to set their prices individually.

Box 6: Regulations endorsing price fixing by the airline association in Indonesia

Anticompetitive Regulation

In Indonesia the airline industry consists of a number of state-owned enterprises as well as private businesses. Airline tariffs are regulated by two Decrees of the Minister of Transportation. One of these decrees previously provided that the Indonesian Airlines Association (INACA) —which at the time of writing consisted of 15 member airlines - could establish scheduled passenger tariffs on domestic economy class routes.

The pricing mechanism used by INACA involved gaining the consensus of all of its members before consulting with the Minister of Transportation. The INACA price was then used as a reference by members in setting the airlines' tariffs.

Harm to Competition

The INACA price was generally set above the market price thus raising prices for consumers.

Following an investigation by the Indonesian Commission for the Supervision of Business Competition, the delegation of the price mechanism to INACA and the agreement among its members was found to constitute a cartel and was therefore potentially in conflict with Indonesian law.

Procompetitive Solution

The right and authority for INACA to establish tariffs was abolished by the Ministry of Communication and Transportation through a revision of the regulations. The sector also underwent further deregulation in parallel in order to enhance more fair competition in the airline industry.

Airlines tariffs have been drastically reduced as a result of the above actions, falling by around 50 percent. The airline industry has become more competitive and utilisation levels have also increased as a result of increasing demand.

Source: Iwantono, S (2003). Economic Crisis and Cartel Development In Indonesia, KPPU, Presented at: Vth International Cartels Workshop, Brussels.

Box 7: Proposed price caps in Kenya's telecommunications sector

Anticompetitive Regulation

In 2011, a proposal was made to regulate a basket of telecommunications services in Kenya by subjecting these services to retail price caps.

Harm to Competition

The ex-ante regulation of retail prices is generally considered to be distortive of downstream market competition, and may lead to slow investment, innovation (launch of new products) and growth.

Procompetitive Solution

In vertically related markets, problems at the retail level are typically least distortively resolved through effective remedies imposed at wholesale level leaving the retail market open to the competitive process. In general, regulation should occur at the highest possible level of the value chain in order to let competition develop as much as possible in downstream markets.

Effective wholesale regulation should significantly reduce barriers to entry into the retail market, allowing new entrants to provide retail offers based on wholesale access to the networks of incumbents.

In this case, rather than regulating retail tariffs, the CA ultimately opted to mandate a cut in interconnection tariffs (the amount charged by a network operator for terminating a call from another network on its network) from KES 2.21 to KES 1.44 in 2012. This reduces the costs of small players and has the potential to enhance competition. Interconnection tariffs have now been falling in Kenya since 2010 and this has been largely credited with the observed reduction in final mobile tariffs over that period.

Any remaining anticompetitive issues in the market can be combated by:

- Increasing competition by reducing barriers to entry. For example, the Communications Authority of Kenya[1] (CA) has powers to license more operators if the current number was deemed to be insufficient for effective competition.
- Applying the Competition Act ex post to sanction and deter anticompetitive behavior.

CAK and the Communications Authority of Kenya have also developed a Memorandum of Understanding (MoU) to provide guidance in the handling of jurisdictional overlaps on competition issues.

Source: CAK
http://www.businessdailyafrica.com/Corporate-News/Safaricom-biggest-loser-as-CCK-cuts-termination-rate-/-/539550/1629936/-/item/1/-/hhpx28z/-/index.html

Box 8: Setting of a minimum advocates' fee in Kenya

Anticompetitive Regulation

Under Section 44 of the Advocates Act, the Chief Justice (CJ) is authorised to prescribe and regulate the remuneration of advocates "as he thinks fit". The Act empowers the CJ to issue an Advocates Remuneration Order, which sets the minimum fees that an Advocate may charge for services. The Advocates Remuneration Order provides that "No Advocate may agree or accept his remuneration at less than that provided by this Order."

Harm to Competition

The setting of a minimum fee restrains competition within the legal profession since law firms capable of providing services at lower fees would be constrained from expanding business by providing cheaper services.

The competition law states that "a professional association whose rules contain a restriction that has the effect of preventing, distorting or lessening competition in a market may apply in writing ...for an exemption". The Authority can grant exemptions only in cases where public benefits outweigh detriment to competition Efforts are underway to increase the awareness of various stakeholder agencies on the stance of Kenya's competitions policy towards the fixing of a minimum fee.

Source: CAK

Box 9: Review of the National Cereals and Produce Board in Kenya

Anticompetitive Regulation

A recent market inquiry by CAK into the maize sector and the rising maize prices witnessed in 2010/2012, cast light on the potential harm to competition that may arise from the National Cereals and Produce Board (NCPB), a State Owned Enterprise.

Since liberalisation of the maize sector, the Government has contracted the purchase of a given quantity of maize to the NCPB to form the Strategic Grain Reserve. This forms part of a price stabilisation mechanism and is run alongside NCPB's commercial activities.

Harm to Competition

The NCPB's purchase of maize is not carried out under competitive conditions, with the NCPB making direct purchases from mainly large-scale farmers with no tendering procedure. Moreover, the NCPB currently purchases locally produced maize grain at a fixed price which is frequently higher than competitive market price. Jayne et al. (2008) estimate that NCPB actions from 1995 – 2004 are estimated to have contributed to an increase in the price of maize grain by approximately 20 percent on average during the same period. In addition, the same study found the maize marketing policy pursued by the Government through the NCPB led to a reallocation of income from urban consumers and a majority of small-scale households (net buyers of maize), to a relatively small number of large--scale farmers (sellers of maize).

A recent study estimated welfare gains in Kenya from a 20 percent fall in the price of maize and found that the poorest decile stand to gain 6.4 times more than the richest (Argent and Begazo, 2014). It stands clear that a decline in maize prices will substantially benefit the poor.

Moreover, the current policy framework is likely to alter the competitive conditions in the market. First, farmers' production decisions during growing season will be influenced by expectations of NCPB's post-harvest activities. In addition, although the NCPB operations have a direct impact only on the upstream market, its activities will also change market conditions, indirectly affecting prices and expectations for smallholders, at the milling level by affecting the cost of inputs, and in the downstream market

Procompetitive Solution

Whilst price instability is one of the main issues that drive the NCPB's involvement in the staple food sector, there are a number of less restrictive, market-based, policy options to ensure price stability. For example, within the market framework, the development of commodity exchange platforms would represent a market alternative to manage price instability and risks.

As a step towards reforming NCPB, in July 2013, a Presidential Taskforce on Parastatal Reform recommended that the board should be restructured to separate its commercial and social functions by transferring the Strategic Grain Reserve mandate to the Ministry of Agriculture, Livestock and Fisheries, whilst NCPB would be retained as a purely commercial entity.

Source: CAK

Box 10: Review of the Cereal Millers Association in Kenya

Anticompetitive Regulation

The Cereal Millers Association (CMA) is a private sector association for the millers of maize, wheat and other cereal crops. As part of CAK's recent market inquiry into the maize sector, the activities and regulations of -were assessed in terms of their effect on competition. The association's internal regulations were found to contain provisions which could be potentially harmful to competition, relating to the harmonisation of prices, establishment of agreements, and exchange of information.

Procompetitive Solution

CAK took action to address the CMA's regulations and practices by:

- Ordering the amendment of the objects of the Association's Memorandum and Articles of Association to be in conformity with the Competition Act; and
- Issuing 'stop and desist' orders on arrangements for price coordination.

Source: CAK

ii. **Limits on freedom of firms to advertise or market their goods or services.** Regulations related to advertising are often enacted in order to limit false or misleading information being given to the public. Such regulations can also protect consumers from consuming harmful products such as tobacco or alcohol. However, restrictions on truthful advertising that do not clearly meet such objectives need to be scrutinised. Restrictions on advertising can be detrimental to new entrants to the market because they are unable to inform customers of the services they have to offer. Advertising also plays a role in allowing consumers to make better, more informed, choices (see Section 7 for further details).

Box 11: Advertising restrictions in professional services in Europe

Anticompetitive Regulation

The use of advertising and marketing of professional services is often regulated. In the past, regulations, including self-regulation, varied from the regulation of certain aspects of advertising to a total ban on advertising. In Ireland, for example, there is still a total ban on advertising for barristers.

Restrictive rules may relate to particular forms of advertising, such as television advertising or 'cold calling', or the contents of the advertisement (such as, advertising special expertise) or by restricting the means by which consumers can solicit help for themselves (for example, by submitting a request for help to a web-site that distributes these requests to member lawyers).

Procompetitive Solution

Total advertising bans are increasingly being put under great pressure by consumer organisations and competition authorities. The European Commission, for instance, has clearly stated that advertising should be allowed as a legitimate means of competition when it is based on verifiable and representative information.

Meanwhile, a study by the Maastricht Accounting and Auditing Research Centre concluded that there is no evidence that restrictions on advertising by auditors make a direct, positive contribution towards audit quality. They concluded that there is convincing evidence on the negative effects of these restrictions on intra-EU competition. The study recommended that national restrictions regarding unsolicited offering of services and advertising should be removed.

An alternative to advertising restrictions would be to focus on preventing untruthful or misleading advertising. This objective could be achieved by setting up a mechanism where consumers can file their complaints and where penalties are imposed for fraudulent or misleading advertising. For example, comparative claims in Taiwan have to be validated by an independent authority.

Sources: OECD (2009), Competitive Restrictions in Legal Professions. OECD (2011), Competition Assessment Toolkit, Version 2.0

iii. **Standards for product quality that are above the level that some well-informed customers would choose.** Consumer welfare can be reduced by such standards because consumers are prevented from buying lower price, lower quality goods that they would prefer, even when fully informed of all associated risks. Low-income consumers are particularly likely to be negatively affected by this outcome.

The added costs of delivering unduly high standard or quality products need to be carefully considered, as the higher costs incurred by businesses will typically translate to higher prices paid by consumers, and reduction in the variety of products and services available. For example, food and beverages clearly need to be safe for consumption, but pushing quality and content to higher than necessary levels can have the effect of reducing the variety offered to consumers and raising prices. Likewise, housing and construction codes are necessary, but setting standards too high and limiting supplies of buildable land could lead to considerably higher housing prices that may result in many lower-income individuals being denied access to the market.

In setting standards, rules need to be set and applied to the very specific types of content or issues deemed harmful. Otherwise there may be a tendency to apply the restriction more broadly, risking loss of variety and harming competition. Furthermore, ensuring quality through performance-based standards is preferable to using prescriptive standards,because suppliers have flexibility to tailor their product characteristics provided they meet the performance standard, leading to more choice for consumers. For example, pollution controls on car emission limits are preferable to restrictions on engine capacity limits since they will introduce incentives for producers to develop technology that minimises pollution.

Finally, it should be borne in mind that seller reputation can safeguard quality without the need for regulatory intervention, particularly where consumers can observe quality and make repeat purchases.

iv. **Restrictions on any firm's operations, production processes, procurement processes or on its choice of organisational form, including restrictions which limit the scope for innovation to:** (a) introduce new products; (b) supply existing products in new ways (using different marketing channels or different formats, for example); or (c) procure products in new ways (using different procurement channels, for example). Policies that restrict the production or marketing processes may have social objectives such as the protection of employees or environment. However, such policies may limit the freedom and ability of producers to innovate and invest in new production processes or marketing channels and, as a result, producers may become less efficient, with adverse effects whether on product quality or the prices paid by consumers.

For example, in addressing environmental concerns, relying on technology-based regulation – which requires firms to adopt certain technologies - has the disadvantage of discouraging the development of alternative, more efficient production methods. Meanwhile, performance-based regulation –which sets a level of performance but allows for flexibility in how that level is reached –provides greater incentive and opportunity for innovation.

Regulations can also restrict the type of products that can be sold, or services that can be offered, or the format in which they are sold. Such restrictions often apply to the retail and tourism sectors and can include, for example, regulations on opening hours or on the number of days per year that a service can be provided, regulation on the physical characteristics of facilities or vehicles used to provide a service, or restrictions on the offer of special promotions, such as the time period for which they can be offered. In the transport sector, restrictions on backhauling (i.e. hauling cargo back from a destination point to the originating point), or restrictions on intermodal operations (i.e.,links between companies operating in different transport sectors) can also limit the types of services that can be offered. These restrictions impair the ability of providers to compete in catering to customers' desires and may reduce the variety of goods and services available to consumers.

Furthermore, these types of restrictions may arise where licenses or permits are granted for such specific activities that they unnecessarily constrain firms from adapting to changing consumer demands and market conditions by venturing into new activities and services or modifying existing activities.

v. **Self-regulatory or co-regulatory regimes vesting excessive powers in incumbents.** Self-regulation takes place when a professional or business association is solely responsible for managing the conduct of its members. Co-regulation exists when the government provides legislative backing to rules that are developed at least in part by the professional association. In some cases, membership in a professional association is a requirement in order for a firm to enter a market. Professional associations may adopt rules that reduce competition. The government should retain powers to thwart such attempts. This may include ensuring that the self-regulation or co-regulation is subject to competition law enforcement, and that the relevant governmental authorities have the right to approve or refuse association rules.

Boxes 12 and 13 outline two cases where issues were raised by incumbents' involvement in the licensing process for new entrants.

Box 12: Restriction of entry by incumbents in Kenya's tea sector

Anticompetitive Regulation

Requirements for the licensing of new tea factories contain several potentially restrictive requirements. For example, the TBK has established a condition that existing factories must provide a "no objection" before a license issued to a new factory. This implies subjecting the entry of new tea factories to clearance by market incumbents, placing a degree of discretionary decision-making power in the hands of incumbents.

In addition, prospective licensees for green leaf tea are also required provide proof of having established a minimum of 250 hectares of mature tea bushes in order to obtain a license. These excessive requirements may have a negative impact on competition as they create significant barriers to entry.

Harm to Competition

In October 2012, a private investor lodged a complaint with the Competition Authority of Kenya alleging that tea factories affiliated to the Kenya Tea Development Agency (KTDA) had objected to its entry into the market,and the Tea Board of Kenya (TBK, the tea sector regulator) was therefore objecting to it being licensed. The investor alleged that the incumbents had raised unreasonable objections to the granting of its application to construct a Specialty Tea Factory and that the regulator did not have valid grounds to decline grant of the license.

Procompetitive Solution

Potential actions to enhance competition in the tea sector include:-

- The TBK could allow market forces to determine the allocation of resources in the tea sector, without the involvement of incumbents in entry decisions, in situations where such markets are contestable.
- The National Tea Policy under development by the Ministry of Agriculture could refrain from containing rules or requirements that unreasonably restrict competition.
- The Tea Act and draft Tea Regulations could be reviewed to remove unrealistic requirements on farm size and factory licensing, which effectively create barriers to entry which impose costs which outweigh benefits of such restrictions. For further discussion on this, please refer to Section 4. (iii) on barriers to entry as a result of licensing requirements.

Source: CAK

Box 13: Incumbent involvement in ship licensing procedures in the Philippines

Anticompetitive Regulation

Ship licensing procedures traditionally contained "a prior operator rule" that allowed incumbents to challenge a potential new entrant. The licensing procedures included a public hearing where incumbents are specifically invited to comment on the entry of new firms, based on economic arguments. In addition, the licenses are also very restrictive in terms of the routes, schedules and vessel activity that ships can operate. Firms desiring to modify their existing licenses will also be subjected to challenge by the incumbents on those new routes.

Harm to Competition

The licensing process creates a competitive barrier for firms to quickly enter markets, as well as to redeploy vessels when market conditions change. It is thought that, as a result of this, shipping services in the Philippines have traditionally been relatively expensive and inefficient, and competition across the majority of major routes has been limited to one or two players.

Procompetitive Solution

In 2014, the Maritime Industry Authority (MARINA) passed new regulations designed to curtail incumbent involvement in licensing decisions. Incumbent firms are no longer invited to attend the public hearings, and MARINA will no longer accept challenges related to firm entry based on economic arguments. In addition, MARINA has also streamlined ship licensing procedures to minimise bureaucratic procedures, and allow for greater flexibility within the license itself.

The elimination of the prior operator rule will allow for the easier entry of firms into highly contested routes. The reformed procedures allow for the licenses to be obtained within two weeks (rather than the previous period of up to six months). Removing barriers to entry in the shipping sector is expected to generate an expansion of business by existing shipping companies as well as the potential entry of new market players, which in turn would lead to lower freight rates and better quality of services. Moreover, MARINA can eventually redeploy resources that were previously focused on market regulation towards higher value activities such as vessel safety and environmental protection.

Source: WBG

vi. **Requirements that information on firm outputs, prices, sales or costs be published.** Though such regulations are often adopted to improve consumer information, they should be avoided if cartel formation is likely in the market. Information published in aggregate without revealing firm identities may be more beneficial. Box 15 in the following section outlines an example of where disclosure requirements in Mexico's procurement rules could lead to an increased risk of bid rigging.

vii. **Introduction or amendment of intellectual property regime.** A change in the design of the intellectual property regime has implications on incentives for future innovation and competition. Policy and regulation variables in intellectual property that can affect competition include the duration of exclusivity, the breadth and scope of the intellectual property right, its associated novelty threshold, the compensation regime, and the methods available for challenging the right (for example, litigation). The strengthening of an intellectual property right to increase incentives to innovate may have an adverse effect on competition by potentially benefitting incumbents to the detriment of new entrants.

Policy makers advising on policies or regulations relating to intellectual property rights are reminded that there are likely to be both short-term and long-term considerations. They are advised to contact the CAK for advice at an early stage in policy or regulation development.

viii. **Exemption of the activity of a particular industry or group of firms from the operation of general competition law.** The rationale and conditions for such exemptions need to be examined if they exist in a market. The laws of Kenya prohibit anti-competitive agreements between undertakings, and prohibit dominant undertakings from abusing their market power.4 Policy makers should seek advice from the CAK if they are concerned that a proposed policy or regulation will exempt suppliers from general competition laws.

4 The Competition Act of Kenya, 2010 http://www.cak.go.ke/index.php?option=com_docman&view=docman&Itemid=501

PART 6

RESTRICTIONS THAT DISCRIMINATE AGAINST CERTAIN AGENTS

This category encompasses regulations that establish or create conditions resulting in unjustified discriminatory treatment that reduces competitive neutrality, including:

i. **Explicit discriminatory treatment among market entrants or discrimination against a given type of firm (foreigners, companies from outside particular county, small companies, new players, private firms, among others).** Within this sub-category, some regulations with a particularly restrictive impact benefit companies already operating in a given market, thus increasing the entry cost for potential competitors (Section 4.v. provides further discussion of regulations which raise the cost of entry). However, some policies or regulations can also significantly raise the costs of some of the existing suppliers relative to the other existing suppliers. For example, a policy that imposes modern technology on firms may inadvertently favour new entrants who have already adopted this technology. A policy that specifies a product standard may favour suppliers already meeting that standard over others that are not.

Moreover, in some cases, certain sectors or specific firms are exempted from compliance with particular requirements or regulations. For example, some policies or regulations significantly raise the costs of new suppliers relative to existing suppliers, including regulations or policies that introduce or reinforce 'grandfather clauses'. Grandfather clauses relate to situations where the existing businesses (incumbents) are allowed to continue operations under older rules whereas new entrants are subject to the newly-imposed rules and regulations. For example, new high-rise buildings may have to install fire-extinguishing sprinkler systems, while older buildings are exempt from these regulations. While the cost considerations for not forcing the older facilities to immediately conform to new regulations is a legitimate economic justification, it is important for policy makers to recognize that grandfather clauses which impose asymmetric standards on older versus newer production facilities may impose considerably greater costs on new entrants as well as new capital investments by incumbents. Grandfather clauses can also impair access for new players by limiting resources essential to compete. Box 14 below provides an example of this.

Box 14: Grandfathering of landing or gate slots in airports favours incumbent airlines

Anticompetitive Regulation

The current slot allocation system that controls landing rights at the majority of European airports, requires a carrier to have a landing slot for a particular time of day in order to operate a flight at that time. The slots are allocated using grandfather rights: carriers that used their slots last year have the right to continue using the slots this year.

Harm to Competition

This allocation system implies that inefficient, high-cost incumbent airlines can have access to an airport even though a new more efficient low-cost carrier could use the slot more productively.

For example, the European Commission in its 2000 decision noted that British Airways' stranglehold on the U.K. markets for air transport is reinforced by the substantial portion of the slots it holds in the relevant airports and by the system of grandfathering that currently exists for their reallocation. (See Brueckner, 2004, for details.) Control of landing slots and gate facilities have also been of significant concern to the U.S. Federal Aviation Administration.

Procompetitive Solution

- Grandfather rights can be made subject to a sufficiently stringent "use-it-or-lose-it" provision to reduce slot hoarding and ensure that slots are utilised (i.e. a carrier has to use the slot a certain proportion of the time to keep it in the next period).
- A secondary market for slots could be introduced. This will allow for the reallocation of slots and reduce inefficiencies in initial allocation (although this can lead to a windfall gain for those who hold the slots)
- A slot pool could be created for newly created slots, slots returned either voluntarily or under the 'use it or lose it' condition and slots otherwise unclaimed under grandfather rights.
- Airports could be authorized to introduce an airport charge system to dissuade air carriers from belatedly returning slots to the pool.
- Ensure that future primary allocation processes for any newly created slots are market based and create competition amongst airlines for slots. For example, rules which allocate a proportion of these pooled slots to new entrants could be introduced.
- Strengthen the transparency of the slot allocation process and the independence of slot coordinators.

Source: OECD (2011), Competition Assessment Toolkit, Version 2.0

Box 15 provides an example of where discriminatory treatment against foreign firms in Mexico's public procurement rules can lead to a reduction in potential bidders and therefore less intense competition and a greater risk of bid rigging.

ii. **Related to point (i) are rules having an impact on competitive neutrality between the State involved in entrepreneurial activities and private agents, to the advantage of State-owned enterprises (SOE).** Such SOEs may compete under non-equitable conditions with the private sector to provide goods or services and benefit from exclusivity rights, subsidies, loans, and other advantages.

Box 15: Encouraging competition and preventing bid rigging through Mexico's procurement rules and procedures

The Mexican Social Security Institute (IMSS) spends around US$ 2.5 billion annually on pharmaceuticals and other goods and services. However, the IMSS's procurement regulations and practices contain a number of provisions which have the potential to reduce competition in the bidding process. The revision of these provision could therefore lead to substantial cost savings:-

i. Restrictions on Foreign Bidders

Anticompetitive Regulation: Current procurement rules on bidders' participation can be discriminatory towards foreign bidders and limit their possibility of selling goods and services in Mexico.

Specifically, only Mexican nationals can participate in national procedures, whereas participation is open to foreign bidders as well in the case of international procedures. In the latter case, however, participation may be restricted to nationals of countries with which Mexico has signed a free-trade agreement before participation is opened up to all interested bidders regardless of their nationality. These provisions effectively limit the pool of bidders who may genuinely be interested in selling goods and services to the Mexican government and public agencies, including IMSS. The result is likely to be that buyers end up paying higher prices for their purchases or buying goods and services of lower quality, compared to the situation when there are no restrictions to bidders' participation, because there may be less competition. Moreover, the restrictions contained in the current legislation – by reducing the number of potential bidders – facilitate collusion because it is easier to agree and enforce a collusive scheme when there are relatively few bidders.

Moreover, at present Mexican bidders are granted preferential treatment in the evaluation of bids. This limits the possibility for IMSS and other public buyers in Mexico to obtain the best prices. This discriminatory treatment effectively penalises foreign bidders and imported goods, which may ultimately discourage participation to the tender procedures.

Proposed Solution:

- IMSS and other public agencies would therefore likely benefit if current restrictions to participation were abolished and all qualified bidders, irrespective of their nationality, could participate.
- An evaluation of the impact that opening tenders to foreign participation could have on national suppliers (and in particular on small and medium enterprises) could be conducted to determine the best way of implementing the change.

2. De Minimis Exceptions

Anticompetitive Regulation: An excessive use of the "de minimis" exception by public agencies under the Procurement Act may result in competition being unnecessarily restricted and "value for money" not achieved for these purchases. De minimis exceptions provide flexibility and allow cost savings in the case of small-value contracts or local purchases. However, in the case of Mexico, the overall value of contracts covered by this exception was significant – up to 30 per cent of the agency's annual procurement budget.

Procompetitive Solution:

- The use of this exception by public agencies should be reviewed to find an appropriate balance between the flexibility and cost savings afforded by such exceptions with the need to obtain "value for money" through a fully competitive process
- Procurement regulation on the size and scope of this exception may be adjusted to ensure the correct balance in achieved.

Public notice and disclosure requirements facilitate bid rigging

Anticompetitive Regulation: The mandatory requirement to hold a clarification meeting for each call for tender may represent an opportunity for bidders to know the identities of their potential competition and exchange sensitive information or reach a collusive agreement. The Procurement Act at present requires that public buyers hold at least one clarification meeting to address bidders' queries about each call for tenders. In addition, current disclosure requirements (e.g. relating to the identities of bidders and the value of the bids they submit) can facilitate bid rigging.

Procompetitive Solution:

- These disclosure requirements should be eliminated from the regulations wherever possible.
- Some jurisdictions specifically prohibit disclosure of the identity of potential bidders and group meetings involving bidders.
- Where elimination of the opportunity for bidders to meet and interact is not feasible, such practices should be minimised and carefully monitored. For example, clarification meetings can be held virtually using remote technology to eliminate on-site meetings. Other alternative methods of receiving bidders questions and sharing responses to those questions amongst bidders without disclosing the identity of other bidders could also be developed by procuring agencies.

Source: OECD (2011), Fighting Bid Rigging in Public Procurement in Mexico

Box 16: Proposals to limit private participation in shipping services in Egypt

Anticompetitive Regulation

In 2013, a reform bill to the Maritime Law was proposed which contained provisions prohibiting foreign companies and imposing significant limits to market participation by domestic players.

Harm to Competition

The Egyptian Competition Authority identified these anticompetitive restrictions and highlighted to the Ministry of Transport that the reform would seal off state-owned shipping agency services from any effective competition.

Procompetitive Solution

As a result the promulgation of these provisions was prevented and foreign and private actors remain in the market for shipping services.

Source: World Bank (2014), Changing Mindsets to Transform Markets: Lessons Learned from the First Annual Awards in Competition Policy Advocacy

iii. **Wide discretionary decision-making powers held by authorities which may result in discriminatory treatment.** This includes all regulations that fail to specify objective requirements for awarding licenses or that create oversight mechanisms providing unlimited powers to decide on suspension of business activities and other similar measures. This type of regulation prevents effective control of authorities' performance and accountability, and therefore may allow the granting of unwarranted preferential treatment to certain players. In turn, this may result in discriminatory treatment among companies competing in the same market and create a culture of corruption. An example of discretionary treatment of registration applications for the agricultural input market in Honduras is provided in Box 17.

Box 17: Registration in agricultural input markets in Honduras

Anticompetitive Regulation

The market for agricultural inputs in Honduras has traditionally been characterized by the discretionary treatment of suppliers in registration applications. This has partly resulted from regulations that were implemented in a way that lacked transparency and predictability. This, coupled with cumbersome registration procedures, meant that some applications were processed in six months, whilst others took three years.

Harm to Competition

Although intended to ensure the safe use of fertilizers and pesticides, this discretionary and cumbersome registration procedures delayed the entry and commercialisation of new and potentially safer products, created unpredictability within the registration process, and limited competitiveness of small and new firms. This is one reason put forward for the high cost and limited quality and variety of key agriculture inputs in Honduras when compared with neighboring countries.

Procompetitive Solution

- Based on recommendations, the government of Honduras took the following actions:
- Optimised registration procedures for agricultural inputs.
- Enforced process manuals to ensure consistency and equal treatment across applications.
- Developed a web-based database of registered input products (and their associated crops) by firm, with tracking information on the product registration process. Public access to the database is intended provide farmers information on products available in the market and serve as a tool for increasing transparency to limit the discretionary treatment of competitors.

This has resulted in a more streamlined and standardised registration process conducted on a level playing field, with processing times reduced from up to three years to 90 days. There has been a 340 percent increase in the number of products registered annually, expanding choice for farmers.

Source: WBG

iv. **Subsidies, incentives policies,access to limited resources (e.g. land, water, spectrum) and other forms of state support that distort the level playing field.** Subsidies or incentives policies, if not properly designed, might alter the level playing field and provide a cost advantage to a subset of active firms. State support includes subsidies, tax exemptions, concessional loans, land rental below market prices, access to government land, water rights, and spectrum rights, among others. Box 18 provides an example of how rules for spectrum assignment can be designed to avoid distortion of the level playing field.

Before granting incentives it should be determined whether the incentives and the procedure for granting them is the most appropriate and that it minimises potential negative effects on competition.

Box 18: Ensuring a level playing field in the auction process rules for 4G spectrum assignment in Colombia

In 2012, the Colombian competition agency (SIC), worked in collaboration with Ministry of Information Technology (MinTIC) to help design auction process rules for 4G spectrum allocation which would ensure a level playing field in the auction process.

Anticompetitive Regulations

Analysis at the time revealed that the mobile voice market in Colombia was dominated by one operator (with 74 percent share, in terms of sector profits) and characterised by a wide disparity in terms of financial capacity between the dominant operator and other providers.

The original design of the auction process proposed an open mechanism in which incumbents and entrants were both able to bid on two segments of spectrum to develop mobile internet services. SIC concluded this design posed several risks that could hinder competition. The study found that an open, unrestricted auction of spectrum would result in continued market dominance by a single player. Smaller operators and market entrants, who would not have the means to deploy the necessary infrastructure to provide service in the new spectrum, would be deterred from competing against the well-capitalised, dominant provider.

Procompetitive Solution

It was recommended that the plan for allocating the spectrum be adapted to:-

i. Encourage the entry of at least one new operator in the voice and mobile Internet market by dividing the spectrum auction into "reserved blocks" and confining the dominant market player to competing in just one of those blocks with other established telecommunications firms. A separate reserved block would be open only to potential new market entrants.

ii. Include mechanisms for implementing network access (roaming) and infrastructure sharing to expedite a new competitor's entry and position in the market.

iii. Include a forward-looking strategy for new operators to build and deploy their own infrastructure within four to five years of using the spectrum to effectively operate in the market.

Ultimately, the auction process was adapted to specify which operators could bid on available blocks of spectrum, and two blocks were held for bids from entrants and smaller operators. MinTIC promulgated regulations about infrastructure sharing (roaming) and network access, which meant new operators in their early years would face lower costs in providing services than incumbents. A follow-up mechanism was designed to ensure that entrants would develop infrastructure sufficient to enable them to compete autonomously after several years

The result was a more level playing field that allowed two new market entrants to effectively vie for a large and rapidly growing customer base, with the promise of more consumer choice, better service, faster innovation, and lower price.

Source: World Bank (2014), Changing Mindsets to Transform Markets: Lessons Learned from the First Annual Awards in Competition Policy Advocacy

v. **Provisions that allow regulators to provide services in competition with private players.** In some cases government bodies carry out both commercial and regulatory activities and therefore regulate their own competitors, creating conflicts of interest and the ability to enforce regulations that put competitors at a disadvantage.

vi. **Lack of a clear and effective access policy (e.g., non-discrimination, clear conditions, cost-oriented fees) to essential facilities or providing exclusive rights of access to essential inputs to certain players.** In the case of network industries, particularly where vertically-integrated firms operate, ensuring access to essential facilities in a non-discriminatory manner, under clear conditions and, wherever possible, at cost-oriented fees, is key for allowing competition in downstream markets. Box 19 provides an example where potentially discriminatory terms of access to the international calling gateway between the state-owned mobile provider and private mobile providers may contribute to raising the costs of mobile services for consumers. Box 21 describes two competition issues which may arise in the Mobile Financial Services sector relating to access of parties to two essential networks for the market: (i) the network of agents; and (ii) mobile communication networks.

Box 19: State monopoly on the international calling gateway in Zambia

Anticompetitive Regulation

In Zambia, the Government is involved in the telecoms sector at various levels:-

- At the regulatory level, the Ministry of Communications and Transport sets out the legal framework and regulatory policy and the regulator (which is not independent of government) monitors the activities of all market participants.
- At the operational level, the Government directly participates in the market as a mobile operator.

Harm to Competition

This dual role may generate some conflicts of interest and a lack of regulatory neutrality between state-owned versus private firms.

These issues have been proposed as a potential reason for the under performance of the Zambian telecommunications sector: the country has fairly low telecommunications penetration rates and levels of investment per capita compared with other countries in the region.

One specific problem often cited relates to the fact that the state-owned mobile services provider in Zambia holds a monopoly on the international calling gateway and charges a high price for its use. This means that the two private firms have to subsidise their international calls to compete with the state incumbent, which may be hindering their investment in infrastructure roll-out. This also in part explains the relatively high cost for mobile services in Zambia.

Procompetitive Solution

These issues point to the potential need for accounting separation between the various parts of state-owned telecommunications companies. This would prevent practices such as cross-subsidisation – taking excess profits from one service (e.g. international call gateway revenues) and using them to provide another service (e.g. domestic mobiles services) at below cost. It would also allow the regulator to determine whether the state-owned mobile operator is paying the same access fees for the international gateway as the private operators.

Source: Ellis. Singh and Musonda (2010), Assessing the Economic Impact of Competition: Findings from Zambia

Box 20: Prohibition of exclusivity of Mobile Financial Services agents in Kenya's National Payment System Draft Regulations

Anticompetitive Risks

In 2013, the Central Bank of Kenya (CBK), the body responsible for mobile financial services (MFS) regulation, issued the National Payment System (NPS) Draft Regulations 2013 which intend to foster interoperability, improve system stability and safeguard against systemic risk in the mobile financial services market.

One issue which could lead to a restriction of competition in this market is the existence of exclusive clauses in agreements between MFS providers and agent or cash merchants which prohibit agents from processing transactions for customers of competitor MFS providers. These exclusive clauses would have a deleterious effect on the ability of competing MFS providers to build agent networks and would reduce consumer access to MFS agents.

Procompetitive Solution

It was therefore recommended during the consultation process for the NPS Draft Regulations that exclusivity between MFS providers and MFS agents and cash merchants should be explicitly prohibited in the draft regulations and that CBK should approve all standard contracts to ensure that this prohibition is adhered to.

At the time of writing, these recommendations have been adopted in the current NPS draft regulations.

Source: CAK

Box 21: Regulation of access to mobile communication channels for Mobile Financial Service providers in Peru

Anticompetitive Risks

Having access to mobile communication channels, particularly the USSD channel, is essential for the delivery of Mobile Financial Services (MFS).

Thus, parties who do not possess their own mobile communications channel, and who wish to enter the MFS market, rely on being able to use the mobile networks of mobile network operators (MNOs). This can be the cause of competition issues when those MNOs are also active in the downstream MFS market. The MNOs may then have an incentive to either deny access or grant access only at a very high price to their downstream competitors.

Procompetitive Solution

In these cases, telecommunications regulators may have an important role to play in ensuring that MNOs who are also active in MFS provision do not unfairly deny access to their mobile communications channel to any other party who requests it.

The regulator can also help to ensure that access is granted on non-discriminatory and cost-oriented terms. This means that MNOs should:-

i. Not provide access to their mobile channel to their in-house or related MFS provider on more favourable terms than they would provide to any other party

ii. Price access on the basis of cost plus a reasonable profit mark-up.

Where this outcome is not achieved by market, in some cases, it may be appropriate to adopt specific regulation to encourage competition in the MFS market.

Peru, for example, has spearheaded this approach. The new E-Money Law passed in 2013 requires that MNOs must offer all third parties access to their mobile channel on a non-discriminatory basis. The law also authorises the telecommunications regulator (OSIPTEL) to facilitate access to the channel for MFS. Accordingly, OSIPTEL has issued a regulation with provisions that include a resolution mechanism if non-discriminatory access for all parties is blocked.

The Peruvian approach is to allow the market to determine pricing in the first instance through commercial negotiations. Only where MNOs and the third party MFS providers fail to agree on terms within two months, will the third party provider be able to request that OSIPTEL impose of terms of access.

In addition to these provisions, non-discrimination will be enforced by requiring that all contracts between MNOs and third party MFS providers be approved by the telecommunications regulator and are made public.

Source: Mas (2014), Shifting branchless banking regulation from enabling to fostering competition. Alliance for Financial Inclusion (2014), Regulatory Approaches to Mobile Financial Services in Latin America

PART 7

RESTRICTIONS ON CHOICE AND INFORMATION AVAILABLE TO CONSUMERS & PRODUCERS

Though the primary objective of most regulations is to improve the welfare of consumers, the following scenarios could act as impediments to the choice and information available to consumers and producers:

i. **Limits on the ability of consumers to decide from whom they purchase.** Regulations in some sectors-for example, medical services-could limit the choice of suppliers for consumers, thereby reducing the incentives of suppliers to provide good quality service and also limiting the ability of consumers to choose from a wide range of suppliers. Box 22 provides an example where regulatory reform in the pharmaceuticals sector has increased the access of consumers to lower priced drugs.

Box 22: Anti-substitution laws in the prescription of branded drugs

Anticompetitive Regulation

Until the mid-1980s, anti-substitution laws in the US prohibited pharmacists from dispensing a lower-cost generic drug for a prescription written for a brand name drug.

Harm to Competition

An extensive investigation conducted by the Federal Trade Commission (FTC) determined that anti-substitution laws imposed substantial costs on consumers by restricting price competition between large manufacturers producing the same drug. It was reasoned that providing pharmacists with the option of choosing between a brand drug and its generic equivalent would stimulate price competition, without compromising the quality of health care.

Procompetitive Solution

Ultimately, drug product selection laws were passed to allow substitution of therapeutically equivalent but less expensive generic drugs for higher-price brands by pharmacists when filing a prescription that names a specific brand.

A study on the economic impact of this reforms showed that generic substitution on eligible prescriptions rose after the passage of these laws, and that generic substitution reduced consumer expenditures.[5]

In 2012, 84 percent of all prescriptions written in the US were filled with a generic drug, and a generic version of a drug, when available, was dispensed 95 percent of the time.[6] Although the vast majority of those prescriptions were written using the brand name[7], a lower-cost generic was dispensed. Generic substitution laws are estimated to have saved consumers more than $1 trillion in just the last 10 years.[8]

[5] Masson and Steiner, 1985, Generic Substitution and Prescription Drug Prices: Economic Effects of State Drug Product Selection Law.

[6] IMS Institute for Healthcare Informatics. Declining Medicine Use and Costs: For Better or For Worse? – A Review of the Use of Medicines in the United States in 2012. Parsippany, NJ: IMS Institute; May 2013.

[7] Steinman MA, Chren MM, Landefeld CS. What's in a name? use of brand versus generic drug names in United States outpatient practices. J Gen Intern Med. 2007;22(5):645-648.

[8] Engelberg, 2014, Have Prescription Drug Brand Names Become Generic?

In transport, regulations may limit firms from carrying their own private cargo by requiring them to have licenses to do so. This can constrain firms by requiring them to contract the services of a freight operator even when carrying out their own transportation would be more cost effective. These types of regulations also artificially protect freight operators from competition and reduce the incentives to improve their services. Such restrictions have been found to exist in certain states in Mexico.

ii. **Restriction of mobility of customers (producers) between suppliers (buyers) of goods or services by increasing the explicit or implicit costs of switching between suppliers (buyers).** Some suppliers impose high switching costs on their consumers by providing them with long-term binding contracts. This also enables the suppliers to charge high prices for their services. A policy or regulation that imposes minimum contract periods, or a minimum notice period for leaving the contract on customers would make it more difficult for the customer to leave their existing supplier in response to a better offering by a competitor; and suppliers would be less likely to compete vigorously for new clients. While due consideration should be given to legitimate switching costs, there are great benefits to consumer welfare if regulations and policies are introduced that reduce or eliminate unnecessary switching costs. Box 23 demonstrates how competition in the banking sector can be increased by making it easier and cheaper for consumers to repay their loans early. Meanwhile, Box 24 and 25 provide examples of reducing switching costs in the telecommunications sector via mandatory SIM card unlocking and through the introduction of number portability.

Box 23: Legislation on fees for early loan repayment in Romania

Anticompetitive Risks

Contractual provisions in loan agreements often prohibit the early repayment of loans, or which impose high fees for early repayment. These charges raise switching costs for consumers, restrict opportunities to refinance debt, and ultimately restrict customer mobility between loan providers.

Despite a European Union (EU) Consumer Credit Directive being introduced in 2008 which recommended the elimination of early repayment fees, in Romania, banks continued to impose these charges.

Procompetitive Solution

The Romanian government and Competition Council acted on the EU directive by issuing an ordinance which allows all credit holders to repay variable interest loans ahead of schedule without paying a reimbursement fee or commission. The amount charged on fixed interest loans was capped at 1 percent.

In addition, under this ordinance, consumers were also given the right to withdraw from the contract, unconditionally and without justification, within 14 days of signing.

An assessment by the Competition Council's showed that less than one year after the implementation of the rule, the number of refinanced loans had doubled and around 190,000 clients had made early repayments on loans, either wholly or in part. The result for consumers has been a total saving of around €7.8 million.

Source:
http://www.internationallawoffice.com/newsletters/detail.aspx?g=1fbf000e-620b-460e-a49c-8acf8f63bc03
http://www.hbalaw.eu/files/newsletter/2010_02_newsletter_en.pdf

Box 24: Mandatory unlocking of SIM cards in the European Community (EC)

Anticompetitive Risks

Mobile handsets are often 'locked' to the network from which the handset is purchased. This means that a consumer may be unable to switch service providers without replacing their handset. Even where the SIM card could technically be "unlocked," service providers generally impose significant charges for the SIM override service, effectively deterring customer mobility.

Harm to Competition

Locking the SIM card in the handset restricts customers from changing service providers by raising the cost of switching. However, one argument for locking is that it allows handsets to be sold to consumers with subsidies, since locking software ensures that devices will be active for a certain period of time on the network of the subsidising provider and allows the provider to recoup the cost of the subsidy.

Procompetitive Solution

In 1996, the EC's Director-General for Competition informed handset manufacturers and network operators that the EC considered SIM card locking to have anti-competitive effects.

After consultation, manufacturers agreed to modify the SIM lock feature in their mobile phones to enable "unlocking." Service providers were allowed to keep the SIM cards locked in the handsets they sold until the subsidies they had provided were recovered.

Service providers were obliged to make full disclosure to customers regarding the SIM Lock feature and were required to provide information on:-

i The amount of the subsidy;

ii. The time and the commercial terms it would take to recover the cost of subsidised phones; and

iii. How the subsidy could restrict the customer's ability to unlock the SIM Lock feature.

Mandatory SIM unlocking has now been introduced in a number of other jurisdictions including Japan and the US.

Source: http://www.ictregulationtoolkit.org/en/toolkit/notes/PracticeNote/3292
http://europa.eu/rapid/press-release_IP-96-791_en.htm

iii. Lack of information required by either (a) buyers to shop effectively; or (b) suppliers to effectively choose a buyer, especially in the context of new markets. Information about product prices, quality, and safety ensures that consumers are more aware and can make informed decisions at the time of purchase. For example, requirements to include certain information on labels provide consumers with more information about the competing products on offer and therefore could favour competition. Moreover, when consumers are faced with choices in a new product or service market that has been created, they are shopping for something they have never previously bought and of which they have no experience. In circumstances such as this where there is an information asymmetry between supplier and consumers, governments may need to provide information on product choices with a reference point for comparing offers. Box 26 provides an example from the mobile internet market in Moldova of how improving transparency can increase competition between players.

Box 25: Reducing switching costs through mobile number portability

Number portability is the ability of customers to retain their existing phone number when they switch their supplier. In mobile telecommunications, number portability is considered to be an important prerequisite for competition as it reduces consumer switching costs. Lack of portability has the potential to lock-in customers to the incumbents' networks and is an obvious source of market power to established suppliers.

Kenya implemented mobile number portability in 2011, joining 62 other countries around the world who have adopted it, including South Africa and Egypt.

Box 26: Improving transparency on mobile internet prices in Moldova

Anticompetitive Risks

A lack of transparency on the actual costs of mobile internet services in Moldova was found to be limiting incentives for competitors to make their service packages more attractive to consumers.

Procompetitive Solution

In 2011, the Moldovan Competition Council and the National Regulatory Agency for Electronic Communications and Information Technology (NRAECIT) entered into a partnership to determine how consumers could be informed about the effective price they would pay for data service above their data limit and to induce new business practices that would improve transparency on prices in the mobile internet market.

The objective was to help consumers compare services and make better informed choices of their mobile Internet providers and how much to use their services.

As a result, two of the three mobile internet providers subsequently implemented voluntary changes in procedure to ensure that subscribers received notice when they were approaching their traffic limits. These voluntary changes in procedure will become mandatory under new rules being adopted by NRAECIT. Consumers can now compare more easily how much they will actually pay for their monthly mobile Internet use and then choose the best offer on the market.

Source: World Bank (2014), Changing Mindsets to Transform Markets: Lessons Learned from the First Annual Awards in Competition Policy Advocacy

PART 8

SOLUTION DESIGN: A GUIDE TO DEVELOPING PRO-COMPETITIVE SOLUTIONS TO ACHIEVE POLICY OBJECTIVES

These guidelines have thus far set out a general framework for the identification of regulatory provisions which may hinder, distort, or eliminate competition in affected market. The following section aims to articulate a set of principles and guiding questions to help identify the most appropriate solutions that incorporate competition considerations in the design of regulatory provisions in order to remove, or at least reduce, potential anticompetitive distortions.

In practice, each policy goal will match with large number of possible regulatory approaches. Because of the complexities that will inevitably characterise each individual case, it is impossible to create a definitive match between current regulation and solutions. However, there are a number of guiding principles that can be applied across cases.

i. **The most appropriate solution is the alternative that, among those that address the underlying policy objective(s), minimises the resulting competitive restraints.** Relying on this principle will help to ensure that the chosen solution: (i) addresses Governments' policy objectives; and (ii) is coherent with competition issues.

ii. **Market-oriented and incentive-based approaches are generally preferable to direct controls:** Policy makers should consider market-oriented regulatory approaches that use economic incentives to achieve regulatory goals and that afford entities greater flexibility in compliance. Such approaches include fees, penalties,rewards, or allocating property rights.

iii. **Standards / regulations targeting performance or outcome are generally preferable to those targeting design or inputs.** Performance standards and regulations express requirements in terms of outcomes. By contrast, design standards specify the means to achieve those outcomes. Performance standards are generally preferred to design standards since they allow firms to have the flexibility to choose the most cost-effective methods for achieving the regulatory goal, and create an incentive for developing innovative solutions.

iv. **Where market failures arise from inadequate or asymmetric information, remedies which increase the amount of information available between suppliers and buyers present the most effective means of correcting the failure.** For example,one justification cited for the imposition of minimum prices in professional services is the need to ensure quality. However, the issue of maintaining quality is fundamentally an informational problem,because it is a lack of information on the part of the consumer as to the quality of the professionals they are hiring which allows sub-standard professionals to survive in the market place at a given price. Instead of imposing minimum prices - which do not tackle the issue of quality but, on the contrary, allow all individuals to obtain a certain minimum price regardless of the quality of service they offer—a less restrictive and more effective way of tackling this problem would be to develop mechanisms to increase transparency for consumers on professionals' track records and service standards.[9]

v. **It is often more efficient to tackle market failures in the activity in which they occur rather than introducing additional restraints in another sub-sector of the market.** Therefore, when designing a solution, it is important to have a clear idea of the interaction that exists between subsectors of the market under consideration. Suppose, for example, that policy considerations and other specific circumstances suggest the implementation of compulsory licensing schemes at the wholesale level of the value chain, leading to a highly concentrated market. In this case, it would be inappropriate trying to counteract the resulting market power of wholesalers by increasing concentration upstream (at the farmer level, through consortia and other associations) or downstream, at processors' level (for example by limiting their number though a licensing regime). This approach would, in fact, multiply competitive distortions possibly leading to higher inefficiency, lower growth and less innovation both upstream and downstream. Box 27 provides an example from Romania in which policy makers attempted to address a lack of entry in rural markets by restricting the number of pharmacies which can operate in urban areas, thus harming competition in cities.

In applying this principle, it is important to remember that price controls to address market failure at the retail level are generally considered to be less distortive if applied upstream rather than at the retail level itself (as discussed in Box 7 regarding the Kenyan telecoms sector). Rather than being an exception to this principle, this is because high retail tariffs are in many cases a result of a lack of access for retail competitors to upstream essential facilities.

[9] It should be noted, however, that caution should be exercised in facilitating information exchange amongst competitors since this has the potential to facilitate collusion. In particular, information exchange of disaggregated/firm-level information on future variables should be avoided.

Box 27: Restriction of competition between urban retail pharmacies in Romania through demographic criteria

Anticompetitive Regulation

Under Romania's Pharmacy Law the process of retail expansion in urban areas must be in accordance with specified demographic restrictions. According to the law, the demographic restriction on pharmacy establishment range from the ability to open one pharmacy for every 3,000 inhabitants in the capital city, Bucharest, to one pharmacy being allowed for every 4,000 inhabitants in smaller cities. By contrast, there are no restrictions for opening up pharmacies in rural areas.

Harm to Competition

Whilst the stated objective of the restriction is the encouragement of pharmacies in rural areas, this provision has the effect of limiting the number of pharmacies that are able to be open in cities by creating a barrier to market entry.

Indeed, the Romanian Competition Commission (RCC) has received several complaints from pharmacists that wish to establish new pharmacies but are prevented from doing so by the current regulation. This has the potential to affect consumers by limiting competition between players which could otherwise have led to lower prices, increased service quality and greater innovation.

Even in cases where prices of pharmaceuticals are regulated, these restrictions may consumer welfare in the sense that variety and quality of service may be affected.

Procompetitive Solution

The RCC has recommended some possible solutions for encouraging the establishment of pharmacies in rural areas using restrictive measures. For example, the condition for a pharmacy to have its own laboratory could be eliminated for rural pharmacies to reduce the costs of entry. Meanwhile, a possible non-regulatory measure is the introduction a pilot program for the establishment of mobile pharmacies that can serve rural areas where access is difficult.

Source: OECD, (2014), Competition Issues in the Distribution of Pharmaceuticals: Contribution from Romania; Doing Business Romania, Roland Berger Strategy Consultants http://oldrbd.doingbusiness.ro/en/5/latest-articles/all/895/romanian-pharmaceutical-market

GUIDING QUESTIONS TO IDENTIFY PRO–COMPETITIVE SOLUTIONS

Outlined below is a set of questions and issues that provide a first step in identifying appropriate alternatives to some of the most frequently encountered anticompetitive regulations or policies in Kenya. These questions relate to a selection of the categories of regulation identified in the checklist in Section 2 and emphasize the role that the assessment of the underlying policy objective and the evaluation of the likely anticompetitive restraints should play.

It should be noted that the following listings are not exhaustive and their objective is to guide the reader in their reasoning. Users of these Guidelines may also wish to refer to the procompetitive solutions presented in a number of the examples provided in the boxes in order to understand the alternatives available to some specific restrictions and the types of actions which have been taken by policy makers in the past.

Policymakers are encouraged to engage with the CAK on a case-by-case basis to receive further tailored information on the design of procompetitive regulations to ensure that the chosen alternative is the optimal solution for the regulatory objective in question.

1. Regulations which restrict the number or range of suppliers or buyers:

Granting of Exclusive Rights	
Question / Issue	**Solution (non-exhaustive)**
a) What is the policy objective being pursued through the granting of exclusive rights?	
b) Is granting exclusive rights strictly necessary to achieve the policy objective?	**(i) If no: remove exclusivity** **(ii) If yes:** (1) Check whether exclusivity is limited to the activity that strictly requires the elimination of competition (2) Reduce the scope of exclusive rights as much as possible (3) Reduce the duration of exclusive rights as much as possible.
c) In the case of exclusive rights awarded to the state, what justifies state ownership?	The presence of a "public good": **(i) Check whether the good in question really presents the characteristic of a public good (non-rivalry and non-excludability) or rather is simply an instance of positive externalities** (a) If it is a pure public good 1. Limit the activity of the SOE to the provision of the public good 2. Allow the participation of private parties (also through PPP)[10] when possible 3. Introduce some form of competition for the market[11] (b) If it is not a pure public good but a case of positive externality 1. Use less restrictive regulatory measures such as standards or the creation of property rights. (i) The existence of bottlenecks and market power (1) Limit regulation to the activity where market power is inevitable and allow competition in all upstream and downstream markets (2) Consider regulating access imposing FRAND[12] obligations (3) Verify whether the bottleneck can be operated by a private company. Consider: (a) Introducing some form of competition for the market (b) Allowing the participation of private parties (also through PPP) when possible

[10] Public Private Partnerships (PPPs) are business relationships between a private-sector enterprise and a Government agency, with the purpose of completing specific projects to the benefit of society. By opening sectors that are normally dominated by public monopolies to private enterprises, PPPs are beneficial in at least two ways. First, if the selection phase of the private partner is properly administered (i.e. competitive and transparent selection procedures are implemented), PPPs introduce a form of competition into typically shielded markets. Second, the same nature of these agreements (i.e. a public/private partnership) is likely to strengthen projects' efficiency, as the private sector is usually more concerned with cost control and effectiveness. The benefits are often perceived by consumers through lower prices, higher quality, greater innovation, and investment (van Herpen,2002).

[11] Competition for the market is the expression used to describe an alternative way to introduce the benefits of competition in markets where it is efficient to have a single (or a limited number) of suppliers. This is often the case with natural monopolies, or in the presence of externalities or public goods, when there is a risk of undersupply. In practice this consists in the assignation of the right to operate in a specific market or sector through competitive auctions or similar tender procedures, as opposed to an assignation on a first-come, first-served basis. Competition for the market is often accompanied by other regulatory provisions, such as control over prices or tariffs, universal service obligations and similar measures aimed at balancing the exclusive right granted.

[12] The FRAND acronym stands for "fair, reasonable and non-discriminatory". Although FRAND obligations are frequent in access regulation, no precise definition exists. Instead, they need to be defined on a case-by-case basis. The term "fair" usually means not anti-competitive nor unlawful; "reasonable" usually refers to the licensing rates (and need not necessarily translate to "cost-oriented"); "non-discriminatory" refers to the idea of ensuring a level playing field and relates to both the terms and the rates included in licensing agreements. FRAND measures in access regulation are very important. The exclusive control over bottleneck facilities gives a wide choice of possibilities to impede potential and actual competitors. This is particularly true where in control are powerful vertically or horizontally integrated operators (Helberger,2002).

Strict Licensing Requirements	
Question / Issue	**Solution (non-exhaustive)**
a) What is the policy objective pursued though the introduction of licensing procedures?	**(i) Market failures:** (1) Externality: check whether less restrictive regulatory measures such as standards, performance regulation, or the creation of property rights are possible. (2) Information asymmetry: (a) Introduce mechanisms to increase information available to market players. (b) Consider standard-setting procedures, codes of conduct. **(ii) Other objectives:** (1) To ensure minimum efficient scale of production is reached: investigate the reasons whether market forces alone would lead to this efficient outcome (2) To promote consolidation at a specific level of the value chain in order to counteract market power upstream (or downstream): Remove licensing procedures altogether and consider a targeted direct intervention upstream (or downstream).
b) If licensing procedures seem appropriate, check the implementation details:	**(i) What is the scope of the license?** (1) Verify that the license does not extend to ancillary activities that do not require a regulatory intervention. **(ii) What are the conditions set by the regulation to obtain a license?** (1) Remove numerical restrictions whenever possible (2) Set transparent and objective/non-discriminatory criteria to grant licenses (3) Remove excessive redtape and streamline licensing process as much as possible. **iii) Is it possible to trade licenses?** (1) Allow secondary markets when feasible (2) Guarantee that there exist appropriate measures to avoid hoarding.

<table>
<tr><th colspan="2">Tariff and non-tariff barriers to trade</th></tr>
<tr><th>Question / Issue</th><th>Solution (non-exhaustive)</th></tr>
<tr><td>What is the policy objective of the tariff or non-tariff barrier?</td><td>Remove barriers to trade to the extent possible, using alternative regulatory measures depending on the policy objective.

If policy objective is:

(i) Addressing market failures

(1) Asymmetric information: Introduce mechanisms to increase information available to market players

(ii) Equity (price stability or income redistribution) or development and productivity growth (granting resources to move along the technological frontier)

(1) Improve access to credit/insurance markets

(2) Use fiscal policy if feasible.

(See also section on price control and quota setting below)</td></tr>
</table>

2. Regulations which restrict the ability or incentives of suppliers or buyers to compete vigorously

Price Controls or Quota Setting	
Question / Issue	**Solution (non-exhaustive)**
What is the policy objective of the price control or quota?	Remove price controls and quotas to the extent possible, using alternative regulatory measures depending on the policy objective. If policy objective is: (i) Addressing market failures (1) Externality: use less restrictive regulatory measures such as standards, subsidies, or the creation of property rights (2) Market power: Limit regulation to the activity where market power is inevitable and remove price control and quotas in all upstream and downstream markets (3) Information asymmetry: remove price control and quotas and, if necessary, use less restrictive measures such as introducing mechanisms to increase information available to market players or establishing performance standards. (ii) Equity (price stability or income redistribution) or development and productivity growth (granting resources to move along the technological frontier) (1) Improve access to credit/insurance markets (1) Use fiscal policy if feasible (2) Use non-discriminatory voucher systems[13] (3) Improve access to price and trade opportunities information.

[13] A voucher is a bond worth a certain monetary value that may be spent only for specific reasons or on specific goods. This constrain limiting their usage is the essential characteristic of vouchers.

Conduct Regulation	
Question / Issue	**Solution (non-exhaustive)**
a) What is the policy objective pursued by regulating conduct?	**(i) Market failures** (1) Information asymmetry: use less restrictive regulatory measures that favour the dissemination of information and the adoption of signalling strategies (2) Externality: check whether free to choose and informed consumers would be able to enforce virtuous competitive behaviour.
b) If conduct regulation or standard setting procedures seem appropriate, check implementation details:	**(i) … of the standard** (1) Set clearly defined and verifiable standards (2) Choose standards that do not have discriminatory effects (3) Unless specific considerations suggest otherwise, choose standards that are consistent with international best practices, so to avoid hampering international trade (4) Allow multiple standards whenever possible. **(ii) … of the certification body** (1) Set transparent and objective/non-discriminatory certification procedures (2) Remove excessive redtape and streamline certification process as much as possible, while at the same time preserving the signalling value of the certification (e.g. ensure certification bodies are independent and dependable).

1. Regulations which discriminate (or facilitate discrimination) against certain agents:

Incentives, Subsidies and Loan Schemes	
Question / Issue	**Solution (non-exhaustive)**
What is the policy objective of the incentives, subsidy or loan scheme?	**(i) Positive externality** (1) Check whether subsidies or other incentives unduly discriminate among market participants or put some participants at disadvantage (2) Check whether subsidies or other incentives distort the allocation of resources across markets (3) Guarantee that the subsidies do not indirectly limit buyers' ability to choose (4) Remove excessive redtape and streamline grant procedures for subsidy schemes that minimize negative effects on competition (5) Increase transparency of the mechanism to grant incentives/subsidies/ loans and the recipients of those benefits. **(ii) Income redistribution** (1) Improve access to credit/insurance markets (2) Use fiscal policy if feasible (3) Use non-discriminatory voucher systems.

Creation of Property Rights Over Limited Resources (E.g. land, water, spectrum, landing and take-off slots)	
Question / Issue	**Solution (non-exhaustive)**
Creation of property rights over limited resources allows markets to emerge and can effectively address problems of externalities. Key considerations include ...	Concentrate on setting up a level playing field in initial allocation and well-functioning secondary markets,which should ensure an efficient final allocation of resources. In particular: i) Guarantee that property rights are well defined and can be enforced ii) Guarantee that the initial distribution of property rights does not create dominant positions iii) Introduce appropriate measures to avoid hoarding.

Competition Authority of Kenya
Kenya Railways Staff Retirement Benefit Scheme Block 'D', 1st Floor, Haile Selassie Avenue
P.O. Box 36265-00200
Nairobi, Kenya
Telephone: +254 20 2628233
E-mail: info@cak.go.ke
Website: www.cak.go.ke