

Policy- Driven Regulation versus Neutral Competition

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Outline

- Regulation versus general competition law control in network sectors – an ongoing debate
- New challenges – market design and proactive regulation
- An alternative paradigm?
 - Competitive Neutrality (CN)
 - Pros and cons of a general CN framework
- Implications for fairness debate

Ex ante v ex post

- Parameters of debate well known in network sectors
- Asymmetrical regulation to curb incumbent market power in transitional period – e.g. telecoms
- Residual asymmetric regulation of the former incumbent is generally defended on two grounds:
- (1) to protect consumers from monopolistic behaviour because not all markets will move to effective competition at the same pace; and (2) to provide a “helping hand” to entrants by deliberately handicapping the incumbent during the transition period.

Ex Ante v Ex post/2

- Structural re-organisation to prevent discrimination against new entrants – e.g. ownership unbundling in energy sector;
- Aims to promote new entry, competition and lower prices
- May also deal with barriers to exit and mobility issues
- Focuses regulatory control on (monopolistic) network issues – e.g., access terms, conditions and pricing

Ex ante approach still fit for purpose?

- AMP approach intended to be transitional – may create inefficiencies in longer term
- Unbundled entities – once unbundled do not need extensive ex ante regulation
- Network access regulatory [prices and terms] only necessary for non-duplicable facilities – but is concept relevant for ‘platforms’ ?

Ex post competition control preferable?

- Ongoing debate in network sectors
- but 'proactive' regulation needed to shape market as fit for new challenges:
- Example: EC's electricity market design/clean energy package = 1000 pages of draft regulation
- Aims to encourage new entrants (prosumers, aggregators etc) and inter alia, remove barriers created by current EU/national legislation

Current state of play

- Regulated activities/sub sectors/segments co-exist alongside (new or emerging) non-regulated activities:
- Burdens or opportunities for actors?
- Example: Electrical vehicle provision/storage
- Is solution to regulate or leave to general competition law?
- Clean energy package: compromise position

Competitive neutrality

- A forgotten child? Initially adopted in 1990s with relative enthusiasm in Australia, competitive neutrality (CN) had by 2013 ‘fallen off the radar’ .
- Could this concept offer a useful and operational paradigm or benchmark as an alternative to the ex ante/ex post debate?

CN - A Revival of Interest?

- Alternative to state aid control – Brexit implications?
- New generation FTAs - EU/Singapore?
- CN and public service provision – a new dimension and challenge?

CN – WHAT IS IT?

- Traditionally CN deals with SOEs/ government intervention/mixed markets
- Could it be extended to deal with mixed markets in sense of regulated v non regulated actors/sub-sectors/segments?
- Implications for fairness debate?

Unctad project (2011)

- Competitive neutrality is the recognition that significant government business activities which are in competition with the private sector should not have a competitive advantage or disadvantage simply by virtue of government ownership and control. This allows resources to flow to efficient producers and maximises consumer welfare.
- It also forces government businesses to be more transparent and addresses private competitor concerns about equity and the level playing field for competition. It is a minimum condition for effective markets where government is involved.

OECD

- “Competitive neutrality [is a] regulatory framework (i) within which public and private enterprises face the same set of rules and
- (ii) where no contact with the state brings competitive advantage to any market participant” [OECD 2009]

What is it?

- *Competitive neutrality requires that government business activities should not enjoy **net competitive advantage** over their private sector competitors simply by virtue of public sector ownership (Australian CN Policy Statement 2009) .*

OFT

- Competitive neutrality is a minimum condition for setting up effective mixed markets – ensuring that there are no artificial barriers to entry and that outcomes are efficient, given wider policy objectives (OFT 2010).

Role of CN

- Competitive neutrality is often a ‘companion policy’ to the extension of the operation of competition law to the public sector, and it has the same rationale – allocative efficiency
- Literature distinguishes between ‘weak’ and ‘strong’ CN

Netting out the advantages and disadvantages

- Advantages can include:
 - immunity from certain taxes and charges
 - immunity from various regulatory requirements
 - explicit or implicit governmental guarantees on debt
 - concessional interest rates on loans
 - not being required to account for depreciation expenses
 - not being required to pay dividends to the owner of the business (ie the State)
 - not being required to achieve a commercial rate of return on assets
 - the ability to act consistently in a non-commercial manner
 - captive or tied markets
 - effective immunity from bankruptcy and
 - where the government business operates in both monopoly and competitive markets, opportunities for cross-subsidisation

CN as complement to competition law

- CN applies even if entity is not an 'undertaking'
- Case C-205/03P FENIN (Paragraphs 25-26)
- CN traditionally aimed at incumbency advantages in transition to market liberalisation
- Can address issues that are difficult to tackle under competition law – e.g. (unfair) cross subsidisation

Policy Regulation as an alternative to CN

- If Incumbency advantages are too large - allowing potential new entrants and incumbents to compete on the same parameters (that is, have competitive neutrality) would imply that incumbents will always win contracts and no new entry will take place.
- Is it better to encourage entry by private operators into formerly public markets by granting them some (temporary) competitive advantage?.
- If so – should CN be introduced as a policy/benchmark once a sufficient level of entry has taken place and competition in the market is adequately regulated?

CN and Public interest

- If CN could compromise public policy objectives, Australian government can invoke a “public interest” test - ex ante via ministerial decree or ex post (whereupon the onus rests with the government to prove its case).

A broad range of exceptions:

- environmental issues;
- social welfare and equity;
- occupational health and safety concerns; and
- economic and regional development, including employment

Summing up

- Focus on CN is of limited use in resolving discussion as to pros and cons of ex ante policy versus ex post general competition
- Many of the same issues of optimal timing to transition from one paradigm to another remain
- CN may be disapplied in public interest - so this does not resolve the fairness debate
- CN is not likely to offer a useful substitute approach for ex post or ex ante control in network sector

CN as complementary paradigm

- Recasting CN as benchmark for understanding and assessing allocation of benefits and burdens in ‘mixed’ markets [co-existing regulated/non-regulated segments] may be a useful tool to address role/impact of policy regulation in markets in transition.
- CN complements competition policy – shares same economic goals – adding ‘fairness’ to the mix is not helpful.