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**COMPETITION POLICY AND GREEN GROWTH**

-- Note by the Delegations of Denmark, Finland, Iceland, Norway and Sweden --

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## COMPETITION POLICY AND GREEN GROWTH

-- Note by Denmark, Finland, Iceland, Norway and Sweden --

1. Green growth is a concept that involves rethinking economic growth, mainly how economies can grow in a more sustainable way. It has evolved out of a strong and increasing policy emphasis on the development of a new economic and social framework that would enable economic growth and development while at the same time preventing environmental degradation and enhancing quality of life. Thus it has been argued that together with innovation, the greening process can be a long-term driver of economic growth through for instance investments in renewable energy and improved efficiency in the use of energy and materials. Reflecting this new policy focus, the OECD has adopted a mandate to develop a Green Growth Strategy.<sup>1</sup>
2. A successful shift towards the ambitions underlying the green growth strategy can only be achieved through cost efficient and coherent policies. Competition policy has an important role in this context. It is up to the competition authorities to ensure that this relationship receives due attention.
3. Economic theory and empirical evidence support the view that competition is desirable because it contributes to efficiency in economic activity, thereby increasing the welfare of consumers and society. The rivalry between competing firms ensures that only the most efficient and innovative firms develop and stay in the market. While it is difficult to measure the degree to which effective competition affects productivity and the economy more generally, a number of extensive studies have found a link between stronger competition and higher productivity growth. So competition contributes to economic growth.
4. There are also important links between competition and environmental policy. Using market mechanisms is important in green growth strategies, as it allows appropriate prices to be determined. These price signals ensure that the correct incentives are in place for pollution abatement and innovation in green technology. Ensuring effective competition is important in this context, since otherwise price signals reflecting environmental externalities can not be effectively transmitted.
5. Effective competition and low barriers to entry are also crucial to innovation and market dynamics, which again play an important role in achieving environmental goals at a lower cost. Thus, given a well designed environmental policy, competition supports the achievement of environmental goals in a cost efficient way.
6. Environmental regulations, practices or enforcement may affect competition negatively. This in turn may increase the social costs of achieving environmental goals. However, pro-competitive legislation is becoming stronger and is being more effectively enforced in many countries. Thus, one of the challenges the competition authorities face in this regard is to contribute to ensure that green legislation will not affect competition negatively and that, instead, pro-competitive legislation is employed. Various means of advocacy channels can be used towards this aim.

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<sup>1</sup> OECD (2009). "A Proposal for Developing a Green Growth Strategy", (2009)147/REV1.

7. As explained above, the growing political emphasis on environmental policy does impact markets and competition. At their semi-annual meeting in the Faroe Islands in March 2010 the Directors General of the Nordic competition authorities discussed some of the challenges facing their organisations as a result of the shift towards green growth.

8. To establish a common ground for the task of addressing future challenges in this context, they agreed to produce a joint Nordic report focusing on the relationship between environmental and competition policies.

9. Perhaps the most important conclusion to be drawn from the report is that competition policy has an important role to play in the development and implementation of a green growth strategy, and in facilitating a successful shift to green growth. The report consists of three main chapters: First, it explores the relationship between competition policy and environmental policy. Thereafter it takes a closer look at certain environmental policy aspects and some of the conflicts that have arisen or might arise between these and competition policy. Finally, it describes how environmental policies are reflected in the practices of market participants through different green schemes. The report concludes with some forward looking perspectives.

10. A brief summary of the main features and recommendations is presented below. The report is available in an electronic format at the respective competition authorities' websites<sup>2</sup>.

### **1. The relationship between competition policy and environmental policy**

11. Environmental and competition policy share the common objective of safeguarding and promoting social welfare.

12. Effective competition can support environmental policy by allowing price signals that reflect environmental externalities to be effectively transmitted. Competition also reinforces environmental policy in that competition-induced innovation efforts and efficiency improvements may be considered important components in a successful environmental policy.

13. However, environmental policy may harm competition by for instance increasing barriers to market entry. Thus, the OECD recommends that environmental regulatory agencies routinely undertake competition impact assessments with regard to their environmental proposals. The national competition authorities can assist in such assessments, and they must be vigilant in pointing out the restrictive effects on competition of various regulations in the environmental area.

14. Environmental benefits might be argued as a defence for horizontal practices or arrangements otherwise deemed restrictive under competition law. However, there are strict requirements to be fulfilled in this regard. The measure in question must be proportional to its aims. There must also be net economic benefits in terms of reduced environmental pressure resulting from the practices or arrangements, as compared to a baseline where no action is taken, and the expected economic benefits must outweigh the costs. Such costs include the effects of reduced competition, along with compliance costs for economic operators and effects on third parties.<sup>3</sup>

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<sup>2</sup> The Competition Authorities websites are respectively: <http://www.konkurrencestyrelsen.dk/en/> (Denmark); <http://www.kilpailuvirasto.fi/cgi-bin/english.cgi?> (Finland); <http://www.samkeppni.is/samkeppni/en/> (Iceland); <http://www.konkurransetilsynet.no/en/> (Norway) and [http://www.kkv.se/default\\_218.aspx](http://www.kkv.se/default_218.aspx) (Sweden).

<sup>3</sup> See Commission notice: "Guidelines on the applicability of Article 81 of the EC treaty to horizontal cooperation agreements" (2001/C 3/02).

## **2. Environmental Policy Instruments and Competition Implications**

15. Governments can choose between two broad categories of policy tools in seeking to respond to and correct for negative environmental externalities: economic and administrative policy tools. Economic tools such as taxes and subsidies work indirectly via the price mechanism while tradable permits work in terms of regulated quantities traded in a market. Regulations of a more administrative character are those that include for example specifications of maximum permitted emissions or detailed requirements for products, production processes or technologies. Such approaches are often referred to as command and control approaches.

16. The workings and competitive ramifications of the main environmental policy tools are summarised below.

### **2.1 Taxes and subsidies**

17. Environmental taxes are an important tool for solving the environmental externality problem, not least because direct taxes on emissions are considered economically efficient. Environmental taxes give polluters an incentive to reduce their pollution to the point where further reduction would cost more than paying the tax. There are, however, important challenges. One is to determine the correct tax level. Another relates to the fact that efficiency requires all polluters to face the same tax level at the margin. Tradable emission permits can resolve the problem of how to determine the correct environmental tax level, provided that certain requirements are met.

18. Subsidies can refer to a variety of transfers, payments, supports (such as tax exemptions) and protections associated with government policies. When considering the introduction of subsidies as a means of achieving environmental goals, it is important to conduct a broad analysis of the net effects on welfare before reaching a decision. Conversely, environmental policies that involve the elimination of environmentally harmful subsidies are generally in line with competition policy.

### **2.2 Tradable emission permits**

19. The EU Emission Trading Scheme (ETS) is regarded as one of the cornerstones of EU climate policy. The price of tradable emission permits plays a role similar to that of a tax. In the ETS, the total number of permits issued and the marginal abatement costs together determine the price for carbon emissions. Thus, for a given total quota, the actual carbon emissions price is determined by the market. The Nordic competition authorities have on several occasions argued that emission permits in general should be auctioned and should cover as many emission sources as possible, and also that incumbents should have no preferential treatment compared to newcomers.

20. For an emission trading scheme to function properly, competition in the permit market must be effective. When auctioning emission permits, auction design is important to ensure efficient pricing and avoid collusion. Thus, the competition authorities must seek to deter and detect collusive practices before, during and after the auction process.

### **2.3 Green public procurement**

21. Public procurement is in itself a powerful tool, given its size in relation to GDP in the respective Nordic countries. Green public procurement (GPP) can hasten the development of markets for green goods. But a certain amount of caution should be exercised before it is used.

22. GPP should only be used if the external effect is not internalized by other regulatory instruments. If other regulatory instruments fulfil the object of internalizing an external effect, adding further regulatory

instruments, for instance by imposing environmental criteria in public procurement may lead to inefficiencies from a socio-economic point of view. If the external effect is partly internalized by other regulatory instruments, GPP could be used and be designed to complement the policy tool in place.

23. It is also important to be aware that GPP can have a negative impact on competition if the restrictions imposed lead to significantly fewer firms being able to submit bids. This may increase the costs for the procuring entities. GPP can also lead to higher prices due to investments being required to enable actors to submit bids. Finally, if the use of GPP is to have a real impact on the environment, it is important that the procuring entity identifies product groups for which there is considerable procurement and that the volume of product used actually has a significant impact on the environment.

24. More fundamentally, the criteria and procurement process must comply with the basic principles of European Community law on public procurement, including non-discrimination, equal treatment, transparency, proportionality and mutual recognition.

#### ***2.4 Restrictive effects of green measures and the importance of advocacy***

25. The transition to green growth implies that a host of green instruments will be implemented in many different areas. Promoting correct pricing of environmental goods is crucial to a cost-efficient environmental policy and proper innovation incentives. This can best be achieved through effective competition, since otherwise price signals reflecting environmental externalities cannot be effectively transmitted. Thus the competition authorities have the essential task of advocating market based instruments in environmental policy.

26. Competition authorities also have an important role in identifying and analysing regulations that may unduly distort or restrict competition. When assessing the competitive impact of specific regulatory green measures, the OECD Competition Assessment Toolkit offers valuable guidance, both for the competition authorities and the relevant sector authorities. In many instances, green measures can be restructured to minimise harm to competition.

27. Furthermore, competition authorities should advocate green measures that are less distorting to competition and endeavour to promote an efficient compromise between competition and environmental policy where appropriate. This role of the competition authorities may also contribute significantly to the task of improving regulatory quality in the environmental area.

28. To succeed, initiatives must be timely, and political support should be sought. In addition, it is clear that changes take time and therefore perseverance may be required.

### **3. Business practices in green markets**

29. Environmental policies can be reflected by business practices related to various green schemes, for instance recycling or waste management or different certification arrangements. Many of the schemes have given rise to concern from a competition policy viewpoint. However, many of them can be designed in such a way that competition in fact supports environmental goals more cost efficiently.

#### ***3.1 Antitrust and green markets***

30. In the European Commission's guidelines,<sup>4</sup> the section focusing on horizontal environmental agreements, it is stated that, by nature, such agreements should be considered in breach of Article 101(1)

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<sup>4</sup> See Commission notice: "Guidelines on the applicability of Article 81 of the EC treaty to horizontal cooperation agreements" (2001/C 3/02).

TFEU if the cooperation does not truly concern environmental objectives but serves to conceal anti-competitive practices. And even though a particular environmental scheme may be endorsed by the authorities, this can not be used as an excuse for practices implying abuse of dominance.

31. Although some cases may be relatively clear-cut, there may be a host of borderline cases. Moreover, it is possible that even though some particular environmental agreement may raise concern from a competition point of view, i.e. since the agreement falls under Article 101(1) TFEU, or the national equivalents, the agreement might also bring economic benefits. These benefits may even at individual or aggregate consumer level outweigh the negative effects on competition. For this to be the case, it should be clear that the measure cannot be achieved through less restrictive means, i.e. that it is proportionate to the aim. The economic benefits should furthermore stem from reduced environmental pressure resulting from the agreement, as compared to a baseline where no action is taken, to pass the test in Article 101(3) TFEU, i.e. the expected economic benefits must outweigh the costs in terms of reduced competition.

### ***3.2 Restrictive practices in recycling and waste management***

32. Recycling and waste management are booming industries in many countries. Industry wide arrangements through for instance branch organisations or industry-owned schemes have become quite common, and are in many cases endorsed by the environmental authorities. This applies in particular to recycling and waste management. Most environmentally related cases encountered by the Nordic competition authorities in recent years have related to recycling and waste management.

33. As these cases clearly show, while there may be good arguments in favour of industry wide arrangements, including economies of scale, operational efficiency, and avoidance of non-participating producers getting a ‘free ride’, various aspects of these schemes may also cause serious competition concerns through:

- risk of spillover effects,
- bundling of demand, and
- pricing and fee structure.

34. The cases also show that in many instances, there are alternative approaches based on competition, or at least approaches involving a less restrictive impact on competition, via which the environmental authorities can reach their objectives in a more cost efficient way. The competition authorities have important roles, both in applying the competition law to such cases where the anti-competitive effects outweigh any benefits and in advocating competition based solutions more widely.

35. It is also worth noting that a significant share of the considered by the Nordic competition authorities related to green schemes have been closed through the application of ‘soft enforcement’, where the elements in the schemes causing concern were changed voluntarily in response to the views expressed by the competition authorities.

### ***3.3 Certification arrangements and competition concerns***

36. Product certification highlights the specific characteristics of a product. Certification is primarily used to signify that a product has one or more credence attributes, which are characteristics that are invisible and difficult to judge. For that reason, certification can significantly reduce the transaction costs associated with information gathering. When buyers get more information it will become easier for them to adapt their consumption choices according to preferences. More information may also lead to a better functioning of the market due to increased consumer mobility.

37. Certification has become a key element in marketing organic food products and has also been receiving growing attention in sectors like construction and taxi services. When certification is introduced, producers have a greater incentive to develop product qualities that consumers demand.

38. Businesses may, however, have incentives to influence the certification criteria so that their own products are favoured compared to competing products. Furthermore, increasing the costs to rivals may be attempted, e.g. by lobbying for a narrow product category definition or monitoring mechanisms that disfavour competitors. In cases where the certification standard places foreign producers at a disadvantage, this may have a negative impact on international trade flows and international competition.

39. The effect of certification on welfare depends on how well the certification standard is designed (it needs to be non-discriminatory) and whether effective competition prevails. The competition authorities have an important role in this context through advocacy and, where appropriate, enforcement.

#### **4. Forward looking perspectives**

40. Competition has a significant impact on the efficiency of environmental policy. Consequently, competition policy and the efficient enforcement of competition law should be an integral part of any green growth strategy. Environmental and competition policies share the common objective of safeguarding and promoting social welfare so we must strive to make the execution of environmental policy and competition policy mutually supportive.

41. Experience has shown that existing environmental policies or schemes may restrict competition by raising barriers to entry and limiting incentives or opportunities for effective competition. The Nordic competition authorities have been active in pointing out these limiting effects.

42. The Nordic competition authorities have been firm and outspoken advocates of market based approaches in environmental policy. In the design of market based policy instruments, it is important to consider how well the ‘newly created’ markets will function. If it appears likely that price formation in a newly formed market, for example, will be strongly affected by market power, a different design would be welcome.

43. Competition advocacy and competition enforcement focusing on the restrictive effects of various green schemes on competition will remain an important task for the competition authorities in the future and constitute an important contribution to the overall success of green growth strategies.

44. Advocacy efforts on the part of competition authorities will lend important support to the OECD Ministers’ aim of “establishing appropriate regulations and policies to ensure clear and long-term price signals encouraging efficient environmental outcomes”.

### **Main Points and Recommendations**

- Environmental and competition policy share the common objective of safeguarding and promoting enhanced social welfare
- Effective competition facilitates the transmittance of relevant price signals that reflect environmental externalities. It also ensures economically correct prices of externalities where markets for emission permits are practicable
- Environmental policy involving the abolishment of environmentally harmful subsidies is in general in harmony with competition policy
- Environmental benefits might be argued as a defence for horizontal agreements otherwise deemed restrictive under competition law
  - To be accepted, such arguments must show that the measure is proportional towards its aim
  - The net economic benefits in terms of reduced environmental pressure resulting from the practices or the arrangements must be clear
- Environmental regulation may harm competition, for instance by raising barriers to entry into the market
  - The OECD recommends that environmental regulatory agencies routinely conduct competition impact assessments of their environmental proposals. The competition authorities can assist in such assessments
- In order to maximise social welfare with respect to both competition and environmental policy, we must strive to make the execution of environmental policy and competition policy mutually supportive