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Troubled Times: What Role for Competition and Regulatory Policy?

Abstract

Hard times, occasioned by a prolonged recession resulting in a series of austerity budgetary measures, generate much economic insecurity. How should the State respond? One clear choice is between robustly enforcing competition and regulatory policy and relaxing these policies. What does the international as well as Irish evidence suggest is the result of such relaxation? Could relaxation of competition and regulatory policy provide greater economic security than robust enforcing? If so, at what price? Are there any conditions under which groups or sectors should be sheltered from market forces to provide greater economic security without losing the overall benefits associated with good principles of competition and regulatory policy? Drawing on international evidence this paper addresses these questions. It finds that choosing to relax competition and regulatory policy may deliver transitory benefits but that it is ultimately likely to be an economically costly policy. Even without relaxation, competition and regulatory policy contain provisions that permit otherwise restrictive agreements and regulations to be allowed, but only when the benefits exceed the costs. These well established precedents are contained in Irish competition law. However, the regulatory process in Ireland has, as yet, to fully reflect international best practice in judging *ex ante* regulation. The OECD (2010) report for Ireland contains recommendations to rectify the situation.

1. Introduction

The Irish economy's immediate prospects for growth and jobs are not good.[1] GNP is forecast to increase in 2012 by 0.1 per cent and by 1.0 per cent in 2013, following a decline of 9.8 per cent in 2009, with a very slight recovery in 2010 and a 0.6 per cent decline in 2011. The outlook for Irish growth if the UK and US economies fail to recover quickly from recession and the euro zone does not solve its sovereign and bank debt problems is even bleaker. Unemployment in Ireland is high, having risen from 11.8 per cent of the labour force in 2009, to a forecast level of 14.0 per cent in 2012 and 13.7 per cent in 2013. Employment fell from 1.93 million persons in 2009 and is expected to reach 1.78 million persons in 2012, 1.76 in 2013. People are concerned – quite naturally – about their present and future job prospects both for themselves and their children. For example, will they be able to afford their mortgage payments, their health insurance premiums, and college fees for their children? Enterprises also face considerable uncertainty as to future demand and access to capital. Not surprisingly, given these circumstances enterprises, employees and others, either individually or through representative bodies, seek intervention from the State to help them deal with such economic uncertainty and insecurity.

Ireland has few policy instruments or levers it can use at present to improve economic performance, which is the key to creating growth and jobs and so alleviating concerns over economic security. Monetary policy is not an option since Ireland entered the euro in 1999. Equally, on fiscal policy the State has very limited room for manoeuvre. Fiscal adjustments by the State are likely to see taxes continue to rise and public expenditure to reduce until at least 2015, although the magnitude of the overall consolidation will decline from €3.8 billion in 2012 to €2.0 billion in 2015.[2] The accumulated debt will mean limitations on fiscal policy well beyond 2015. Thus the State will have to respond sparingly to demands for tax breaks, subsidies or other financial assistance to reduce economic insecurity.[3] Indeed, if anything, the State is more likely to be in the business of closing tax loopholes and eliminating subsidies. This does not preclude, of course, reform of the tax system or better evaluation of public investment in infrastructure projects.[4] A more sensible, efficient and fair tax system, for example, is likely to boost economic growth, by minimising collection

[1] The data in this paragraph for 2009 are taken from Durkan *et al.* (2011, Summary Table, n.p.), for all other years from Duffy *et al.* (2012, Summary Table, n.p.).

[2] EU and IMF (2011b, p. 26).

[3] Except, of course, where there is a compelling argument for public intervention.

[4] On tax reform see Commission on Taxation (2009), on evaluation of infrastructure see Morgenroth (2011).

costs and reducing distortions, and thus contribute towards alleviating concerns over economic security.[5]

However, in times of austerity competition and regulatory policy, which are largely off-budget policy instruments, can be seen as a means by which the State can address the demand for economic security.[6] Consider the following example by way of illustration. Suppose the State wanted to support the income of taxi owners/drivers due to the perceived inequity in market outcomes arising from alleged excess supply, easy entry and destructive competition occasioned by the exceptionally adverse economic conditions. Some alternative policy choices might include:[7]

- limiting the number of taxi licences to below the competitive market level and/or permitting only full-time taxi owners or say drivers with 5 years experience to be taxi drivers (regulatory measures); or,
- exempting taxis from competition law to organise the market to ensure 'fair' incomes and fares (a carve out from competition law).

This example shows how relaxing competition and regulation policy can appear, prima facie, as tools which can be used to meet demands for greater economic security and, given their off-budget nature, are likely to be particularly attractive to the State in a time of austerity.

Reflecting about how competition and regulatory policy can be used to promote economic security, there are two quite different and opposing approaches. *First,* and this is the traditional view of competition and regulatory policy, by making markets work well for consumers (including treating businesses as consumers of goods and services) so that markets operate effectively and efficiently. This approach sees that any arrangements that restrict competition, particularly cartels, should be prohibited, with offenders caught and appropriately punished. Likewise it sees that mergers that substantially lessen competition should also be prohibited. The role of regulation would seek to promote cost-reflective pricing and investment decisions in vital sectors of the economy such as electricity, gas and telecommunications, through the provision of a transparent, predictable and stable regulatory framework. The success of these competition and regulatory

[5] Other policies that promote the framework conditions for growth include active labour market policies (e.g., Kelly *et al.,* 2011), boosting firm innovation and productivity (e.g., Ruane and Siedschlag, 2011), and investing in human capital through education (e.g., Smyth and McCoy, 2011).

[6] Regulatory agencies are typically funded in Ireland through a levy on the regulated entities. However, the State funds the body charged with administering and enforcing competition policy, the Competition Authority, out of tax revenue.

[7] This is not to say that these and other policy instruments such as taxation are perfect substitutes. For a discussion of instrument choice, see, for example, Trebilcock *et al.* (1982).

policies is likely to be important not only to the success or failure of individual markets but also to the wider economy. In particular, by stimulating competition and efficiency in the non-traded sector, this will feed through to lower input prices, better service quality and more choice for the traded sector, thus enhancing competitiveness. The result will be to stimulate growth in output, jobs and income. In short, better and improved economic security. This view of competition and regularly policy is consistent with the general framework conditions to promote productivity, competitiveness and growth.

Second, and this is the entirely opposite approach, it could be argued that in troubled times competition and regulatory policy should be relaxed and administered with flexibility and sensitivity to provide economic security to particular groups that are, or appear to be, especially adversely affected by the recession and austerity. In effect, the first (traditional) approach above should be abandoned or substantially loosened in its application. This alternative approach sees that shelter from market forces can help protect jobs and income and thus provide stability and an opportunity for enterprises and individuals to adjust. Such relaxation would, of course, be temporary; once the economy recovers from the recession then the competition and regulatory regime could return to normal. Precedence for such policy intervention in troubled times can be found in the 1930s in the US and, more recently, in the 1980s in Japan.[8] Intervention to provide economic security is analogous to the demand for subsidies or other forms of sectoral protection (e.g., tax expenditures or tax breaks) that would have been provided through fiscal policy intervention.

The issue thus becomes which way should policy go with respect to competition and regulation.

- Should competition and regulatory policy be relaxed to address concerns over economic security in troubled times?
- What does the international as well as Irish evidence suggest is the economic effect of such relaxation?
- Does relaxation of competition and regulatory policy provide economic security? If so, at what price?
- Are there any conditions under which groups or sectors should be sheltered from market forces to provide greater economic security?

[8] In the 1930s such intervention was combined with the erection of trade barriers. In the post-World War II world, with the creation of the General Agreement on Tariffs and Trade in 1946, moves were made to dismantle the trade barriers that were erected in the 1930s.

This paper addresses these issues by drawing on different kinds of evidence including surveys, case studies, meta-analysis and best practice guidelines developed by international organisations such as the European Commission (EC) and Organisation for Economic Co-operation and Development (OECD). While much of the evidence draws on relatively recent events and experience, reference is also made to the experience of the Great Depression because it is the last time an economic contraction as severe and as global as the current one was experienced. The survey, meta-analysis and case studies are used primarily to examine the impact of relaxing competition and regulatory policy, not only in terms of whether economic security is provided, but also at what cost. In contrast, the best practice guidelines are employed in addressing questions related to the possible conditions under which economic security should be provided through competition and regulatory policy.

The paper is divided into four sections, including the introduction. In Section 2 we look at the international and Irish evidence on the impact of relaxing competition and regulatory policy. We examine not only the economic impact on variables such as prices, growth and competitiveness, but also on whether economic security is provided. Attention turns in Section 3 to an examination of competition and regulatory tests that are (or could be) used by the State in this context, drawing in international best practice. Section 4 completes the paper by drawing conclusions in respect of the questions set out above.

2. Relaxing Competition and Regulatory Policy: the Evidence

Gathering evidence on the impact of relaxing competition and regulation is neither easy nor straightforward. Nevertheless, several sources can be used to cast light on this issue. One set of studies looks at the impact of the relaxation of competition and regulatory policies in troubled times, such as Ireland currently experiences. Other research quantifies the impact of breaches of competition policy or the effects of restrictive or lax regulation in more normal times. Implicit in these studies is the view that vigorous enforcement of competition and regulatory policy is the default position and that relaxing competition and regulatory policy is very much the exception.[9] This reflects the fact that troubled times, such as the current deep recession, are unusual events. The purpose of considering the evidence is to see if such relaxation does provide economic security and, if so, at what cost.

9 A number of studies discuss the positive relationship between competition and growth, several of which are cited below. See also, for example, Van Reenen (2011) on the relationship between management and competition.

We divide the impact of relaxing competition and regulatory policy into two broad categories. First, a general relaxation of vigorous competition and regulatory policy, across the whole economy; and second, the exemption of one or more specific sectors from competition policy and/or the introduction of restrictive regulation to, for example, limit numbers in a particular economic activity. While the evidence is for the most part drawn from other jurisdictions, in some instance reference is made to Ireland.[10]

2.1 Reduced Enforcement of Competition Law

Several policy responses are consistent with under-enforcement of competition law in troubled times.[11] For example, the resources allocated to the competition agency could be reduced disproportionately compared to overall reductions in public expenditure. Thus the agency would not be in a position to conduct as many investigations and prosecutions. Competition law could be amended to make it less effective.[12] Thus any investigations that were conducted would have a much lower probability of success. Alternatively the competition agency could be subject to administrative changes which do not have any apparent strategic direction, e.g., reorganised or merged with another agency with little thought or planning.[13] Enforcement activity would be severely hampered by any of these measures and consequently the probability of being caught breaking competition law would be reduced.

There is a considerable volume of evidence on the impact of breaches of competition law. Attention here will be concentrated on cartels, which are commonly considered to be the most pernicious breach of competition law. Ireland is no exception in this regard and the Irish competition agency has identified fighting cartels as its top priority.[14] There is evidence that competition

10 This occurs primarily in the discussion of the impact of restrictive direct regulation.

11 The record of the policy response in this respect in Ireland since the onset of the recession in 2008 to competition policy is set out in Gorecki (2012a). Of the three policy responses identified in the paragraph in the text, only one was arguably pursued in Ireland – the October 2008 proposal to merge the Competition Authority and the National Consumer Agency. There is virtually no documentation publicly available to consider the case for this policy proposal, but nearly four years on no legislative proposals have been published, although some are expected later in 2012. In contrast, in the UK the merger of the Office of Fair Trading and the Competition Commission, together with the reassignment of some of the functions of the OFT, was announced in October 2010, a consultation paper released in March 2011 (DBIS, 2011) and an announcement in March 2012 that the proposed new agency, the Competition and Markets Authority, would be fully operational by April 2014 (DBIS, 2012).

12 For example, breaches of competition law could be redefined to be much narrower, the evidentiary standard required to prove a breach could be raised, and the investigative powers of the competition agency could be reduced.

13 Thus senior managers are likely to become more concerned with turf wars and reorganisation issues than enforcing competition law.

14 “Cartels are the most serious form of anti-competitive behaviour. So stopping cartels remains the Authority’s top enforcement priority.” (Competition Authority, 2011b, p. 5). The EU takes an equally dim view of cartels with the European Commission (2011, p. 5) stating that “… fighting hard-core cartels is … a fundamental pillar of competition policy …”.

enforcement does impact on the extent of cartel activity. For example, a survey of UK businesses by London Economics (2011, Table 1, p.7), for the UK Office of Fair Trading, found that each cartel investigation deterred 28 cartels.[15] Connor and Bolotova (2006, pp. 1133-1134), in a literature survey and meta-analysis of several hundred cartels across a large number of jurisdictions in the European Union, North America and Asia found that the stronger the competition regime, the lower the cartel overcharge. Thus the evidence suggests that under-enforcement of cartel activity leads, not surprisingly, to more cartels and higher prices.

Nevertheless, it could still be argued that cartels are inherently unstable and provide only temporary protection from the crisis occasioned by the recession. Using this line of thought, investigating and prosecuting cartels is likely to be of limited effectiveness. Furthermore, it could be argued that since cartel arrangements are likely to occur under conditions of fewness, tacit collusion (which is very difficult to detect and prosecute) can be substituted for a cartel. However, the evidence is inconsistent with these views as cartels typically raise prices substantially, persist for years rather than months, and have more rather than less members.[16] For example, Connor and Bolotova (2006, pp. 1133-1134) found that prices were raised well above the competitive level – on average, 29 per cent, with a median of 19 per cent.[17] They also find that cartels last, on average, for 8.6 years (*ibid*, p. 1128).[18] Research reported by Veljanovski (2011, Table 2, p. 879), in a study of European Union cartel decisions from late 2006 to 2010, recorded an average duration of 8.9 years. However, these estimates of cartel duration may be too low, if subsequent to investigation/prosecution former cartel members are able to collude tacitly.[19] In terms of the number of cartel members, Hay and Kelly (1974, p. 20) in a study of US cartels between 1963 and 1972, found that the average number of cartel members was 7.25, but this excluded four cases where there were 50 or more cartel members. Case studies

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15 The UK, like Ireland, imposes criminal sanctions for hard core cartel offences.

16 While the evidence reported here comes from a wide variety of sources, it is nevertheless the case that the samples of cartels selected by the various studies are not random. They will depend, for example, on the legal environment. If cartels are prohibited by law it is likely that they will be secret and only those that the competition agency decides to prosecute enter the public domain.

17 However, there were variations depending on, for example, location, geographic scope and time period.

18 The minimum was 1 month, the maximum, 98 years.

19 The limited evidence is somewhat mixed on this issue. Kovacic *et al.* (2005), examine post cartel prices for various vitamins and find: vitamins markets with two conspirators were able to tacitly collude post the cartel, but not in vitamins markets where there were three or more conspirators. It should also be remembered that EU and Irish competition law contains provisions against concerted arrangements which are a looser form of agreement than a formal cartel. For further discussion see Whish (2009, pp. 104-113), that quotes a European Court of Justice judgment that defines such a concerted practice as "… a form of coordination between undertakings which, without having reached the stage where an agreement properly so-called has been concluded, knowingly substitutes practical cooperation between them for the risks of competition." (*ibid*, p. 105).

of individual cartels, such as bromine, ocean shipping and stamp auctions, find cartels can actually raise prices to the monopoly level.[20]

While under-enforcement of competition policy is likely to lead to increased cartel activity through which enterprises are able to ameliorate the impact of the recession through securing higher prices in a less competitive environment, it is also likely to have a number of adverse impacts which have wider economic effects. *First*, under-enforcement as a policy condones or turns a blind eye to cartel activity, which is a criminal offence.[21] Such a policy might lead to increased criminal activity if norms of behaviour of individuals are influenced by such a permissive attitude by the State towards white collar crime.[22] *Second*, using under-enforcement as a way of providing economic security means that there is no attempt to distinguish instances where there may be merit in providing economic security from instances where there is no merit. Essentially enterprises self select where and when to form cartels. *Third*, cartels are long lasting, with the average duration close to a decade. Hence if the cartel is formed – encouraged by under-enforcement – it will not necessarily cease once the economy returns to better (more normal) times.[23] *Fourth*, cartels lead to higher prices over which policymakers have no control. Hence the prices affected may involve goods or services that are particularly important in the budget of poorer consumers or that are used as inputs into exports, resulting in potential damage to a country's competitiveness. These drawbacks reaffirm the traditional case for active competition policy in terms of promoting growth, productivity, innovation, and consumer choice.

In sum, even if under-enforcement of competition policy provides some additional economic security for self-selected sectoral interest groups, it has numerous drawbacks and is an extremely blunt policy instrument.

[20] However, this is not always the case. For discussion see Levenstein and Suslow (2006, pp. 79-82). See Asker (2010) for details of the stamp auction case study.

[21] While it is a criminal offence in Ireland, the US, Canada, and the UK, it is typically a civil offence in other EU Member States.

[22] See, for example, the discussion of Kreizer *et al.* (2008) which shows how norms of behaviour of others effects the propensity to break the law.

[23] On this issue Levenstein and Suslow (2006, p. 67) comment that, "… successful cartels do not break apart in response to demand fluctuations; they develop organizational machinery of some sort that allows them to weather cyclical fluctuations." The authors also note that often cartels have a "rocky start" before being able to manage "periods of sustained collusion for longer periods."(*ibid,* p. 74). Under-enforcement is likely to facilitate the switch from the rocky start to sustained collusion.

2.2 Exemptions from Competition Law: Carve Outs

While under-enforcement of competition law can provide some respite for enterprises from the competitive pressures of the marketplace by lowering the probability that cartels will be detected and prosecuted, it nevertheless remains the case that such actions are illegal. It would be expected that when economic circumstances return to normal so will enforcement. As a result, cartel and other breaches of competition law, even if allowed during a period of austerity, will still be subject to investigation and possible prosecution. Hence enterprises, often with the support of their employees, may request that the State provides a specific legislative exemption or carve out from the application of competition law.

There are, as noted above, historical precedents for exemptions and carve outs. Specifically these occurred in the US in the 1930s and in Japan in the 1980s.[24,25] In the US the New Deal cartelisation policies "… suspended antitrust law and permitted collusion in some sectors provided that industry raised wages above market-clearing levels and accepted collective bargaining with independent unions" (Cole and Ohanian, 2004, p. 781). Industry-wide codes of fair competition were agreed that raised wages and set minimum prices, the latter of which incorporated "… explicit payments to capital" (*ibid*, p. 785). These arrangements covered a large number of industries and were, ironically, enforced by the newly created Antitrust Division of the Department of Justice (Shapiro, 2009, p.4). The evidence suggests that as a result of these New Deal policies "… in at least manufacturing and some energy and mining industries" (Cole and Ohanian, 2004, p. 793) wages and prices were raised significantly. Hence it is clear that those industries subject to the exemption from the US antitrust laws were offered a considerable degree of economic security.

It should be noted, however, that the New Deal had other much less beneficial effects. In fact, it is now considered to have caused significant and lasting harm. Output and employment were restricted in the cartelised sectors, limiting employment opportunities. Wages in the other sectors of the economy were depressed below their steady state level, even though there was normal productivity growth (*ibid*., p. 812). Wholesale prices were raised substantially

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24 In the US the competition authorities have drawn on the record of the 1930s in formulating current enforcement policy. The Antitrust Division of the Department of Justice is "… dedicated to vigorous enforcement of the antitrust laws during these challenging times" (Shapiro, 2009, p. 11). Another difference with the 1930s is that the widespread protectionism that occurred then has not taken place in the current recession. One of the reasons for this is the growth of global supply chains (Datt, *et al.*, 2011). The widespread protectionism facilitated the price increases, particularly in the traded sector.

25 For a discussion of Japan in the 1980s, see Porter and Sakakibara (2004); Porter *et al.* (2000); and, Hayashi and Prescott (2002). The findings are similar to those for the US in the 1930s.

compared with what they otherwise would have been – 24 per cent in 1935 and 14 per cent in 1939 (*ibid.*, Table 5, p. 791). Unemployment was higher than it otherwise would be. In other words, the insiders – those subject to the protection of the codes of fair competition – benefited from the exemption from antitrust laws and associated policies while those outside lost. However, the ramifications extended beyond these redistributive effects to have wider macroeconomic implications. Both Cole and Ohanian (2004) and Romer (1999) argue that these New Deal policies held back the subsequent recovery by preventing adjustment in the 1930s.

2.3 Regulation: Changing the Rules of the Game in Favour of the Incumbent

To a considerable extent enterprises in regulated markets, such as fixed line telecommunications networks, energy networks, water supply and airports, are automatically protected from austerity and economic adversity. They are typically assured of a guaranteed rate of return and protected from competition since they are either a natural monopoly or, at worst, part of a tight oligopoly. That does not mean, however, that these industries are immune from the impact of the recession, since demand for all these areas is likely to be less than it otherwise would be. In the case of airports, for example, demand is likely to be quite income elastic. Furthermore, regulated enterprises might have become highly leveraged and experience problems servicing such debt in troubled times. Incurring such risks may in part reflect a view, given the importance of the regulated enterprise's activity to the wider economy, that the regulator and/or the State would step in to provide assistance if loss of service is threatened due to financial problems. However, a regulatory regime that sees its function in terms of efficiency and consumer welfare may not be receptive to the representations of the regulated enterprise for a more lenient or favourable regulatory regime.

Governments can alter the regulatory structure in a number of ways to assist regulated enterprises and their labour forces, which are suffering either directly or indirectly because of the recession. *First*, the objectives of the regulation can be revised to give greater weight to the interests of producers, broadly defined to include the regulated enterprise, its owners and employees. This is most likely to occur where the regulator is given a statutory duty to promote the industry as well as to promote efficient investment and pricing, the more traditional objectives of sector regulators. Until recently, for example, banking legislation in Ireland had the twin objectives of promoting both financial stability and the financial services industry,[26] while the objectives of the Commission for Aviation Regulation were amended in 2004 to be more favourable to the airport authority.[27] *Second*, the regulatory regime could be changed to give the relevant Minister more control over individual decisions of the regulator. In such a scenario the regulated enterprises and their employees could make direct representations to the Minister so as to influence the regulator's decisions. There can be little doubt that, in the short term at least, such moves provide greater economic security to the regulated network industries. However, there are a number of significant drawbacks for such policies.

First, it is not obvious that regulated enterprises and their workforces merit special regulatory treatment. These industries, as noted above, are frequently guaranteed certain rates of return and are essential services. In some instances, such as electricity, there is some evidence that rents are being earned.[28] *Second*, if there is a concern that a regulated enterprise is in financial difficulty that might result in interruption of a vital service, such as electricity or telephone/data transmission, then the solution is not for a regulatory regime that protects the regulated enterprise from the consequences of its own decisions, but rather the introduction of a resolution mechanism that allows the regulator to intervene and take over the enterprise.[29] *Third*, giving dual objectives to a regulator may hamper effective regulation. What is the correct trade-off between promoting/protecting the regulated industry and promoting more and greater efficiency and consumer welfare? In the case of the Central Bank of Ireland the dual role of the regulator may have led to lax regulatory enforcement that contributed to the size of the financial crisis in Ireland. Other examples of dual objectives that contributed towards adverse policy outcomes include the regulation of the Japanese nuclear industry where the relevant regulator had a role in both promoting and regulating the safety of the nuclear industry[30] and in the UK "… over [BSE] infected beef, [where] a government department responsible for both consumer protection and industry sponsorship voiced misleadingly reassuring statements until the problem because too serious to ignore. The crisis was a particularly forceful example of the dangers of linking

26 See Honohan (2010) for details.

27 See Gorecki (2011a, pp. 195-196) for details.

28 See Diffney *et al.* (2009). The Review Group on State Assets (2011, p. 18) recommended that in view of the widespread public perception "… that remuneration levels and employment conditions in Irish state-owned companies are generous … and that this category of state employees has avoided the consequences of worsening economic conditions nationally," the perception should be investigated to test whether or not it is accurate.

29 For a discussion see Review Group on State Assets and Liabilities (2011).

30 This example was highlighted in a *Financial Times* editorial, with respect to the dual role of the Japanese trade and industry ministry "... which has been responsible for both promoting and regulating nuclear energy. This created a damaging conflict of interest and compromised safety" (Financial Times, 2011, p.8).

sponsorship with regulation. The results were damaging to both the interests of the industry and the interests of the public." (Kay, 2009, p. 35).

Fourth, compromising the independence of regulators can increase uncertainty and result in higher prices for consumers of the regulated service. Investments in infrastructure industries are often long-lived, with asset lives measured in decades rather than years. Furthermore, the assets are frequently capital intensive with a very low if not zero alternative use. In other words, there is a high component of sunk or irrecoverable cost. In making such an investment, a stable, transparent predictable independent regulatory structure will result in project returns being subject to a lower degree of risk, other things being equal. Low risk translates into lower financing costs and prices for the regulated good or service. If, however, the regulatory structure is not independent so that its decisions are subject to revision by Ministerial intervention, particularly with respect to individual investment and pricing decisions, then investors are likely to demand a higher return in view of the higher level of regulatory risk.[31,32] This will ultimately feed through to higher prices. Since many of the infrastructure regulated sectors are non-traded inputs into the traded sector, Ireland's competitiveness will be adversely affected by higher prices. This will lead to job destruction and less rather than more economic security.

2.4 Restrictive Sector-Specific Entry and Price Regulation

In a period of austerity, with concerns over easy and excessive entry, destructive competition, falling standards, bankruptcies and low returns, one tempting response of the government to ensure economic security is to introduce direct or sector specific regulation (direct regulation) in particular areas. Such regulation typically shields incumbents from competition from outsiders/potential entrants by limiting new entry, while restricting competition between incumbents through, for example, specifying prices and other commercial conditions. Such regulation was, at one time, widespread in sectors such as buses, taxis, trucking, and airlines. In the US and Canada, much of it was introduced during the Great Depression and only abolished in the 1970s and 1980s when the impact of such regulation was evaluated and found to be damaging to growth and productivity.[33] More recently the OECD (2001) evaluated such price and entry regulation in

[31] For further discussion of this problem see Gorecki (2011a, pp. 181-188) and references cited therein.

[32] It could, of course, be argued that since the regulated firm is being treated in a more favourable manner that as a result the risk would be lower. However, this need not be the case. To the extent that the regulated market is more subject to political direction then there is always the possibility that either such direction will be used for purposes other than to increase economic security and even where this is not the case there might be some political quid pro quo expected for assisting the regulated firm.

[33] See Breyer (1982) and Kahn (1988) with respect to US direct regulation and Economic Council of Canada (1979, 1981) for the experience for Canada.

Ireland. Many of the same themes and empirical findings that emerged from the evaluation of direct regulation in North America[34] were echoed in the findings for Ireland. In view of this, much of the discussion in this section draws upon Irish examples.

In terms of providing economic security, the international and Irish evidence is consistent with direct regulation limiting supply and increasing prices. While new greenfield entry is typically restricted under such regulation, entry is still possible through purchasing the right to engage in the regulated activity from an incumbent. This might, for example, be a licence in the case of a taxi or a public house. The price that is paid for the right to engage in the regulated activity is a measure of its 'economic rents', i.e., the difference between the return to employing capital in the regulated compared to a competitive sector, adjusted for any differences in risk. It should be noted that qualitative regulation can, to some extent, substitute for quantitative restrictions.[35]

The extent of these economic rents can be illustrated in Ireland. For example, in 2000 the capital value in Ireland of a taxi license traded in the secondary market was €101,000, a public house license €140,000, while prior to road freight deregulation in 1986, a road freight license traded at €40,000.[36] Restrictive entry regulations in the pharmacy market between 1996 and 2002 resulted in a 40 per cent increase in the value of a pharmacy. The impact of airline regulation was to raise prices by between 18-33 per cent. There is also some evidence that the value of licenses increases over time. In the case of a Dublin taxi license, it increased, measured in constant 1980 €, from €4,400 in 1980, to €5,100 in 1985, to €26,000 in 1990, to €37,400 in 1995 and €42,300 in 2000, immediately prior to liberalisation of entry controls. Much of the evidence suggests that direct regulation needs to be measured over decades, because once it is introduced in response to a short-term crisis, it may not be reformed or removed easily. In Ireland, for example, the duration of such regulation is: airlines, 54 years (1932-

[34] On Canada, see Economic Council of Canada (1979, 1981); on the US, Breyer (1982) and Kahn (1988). In the case of taxis, for example, restrictive entry raised rates in Canadian municipalities between 5 and 25 per cent (Economic Council of Canada, 1981, p. 25). This is consistent with evidence for the US where taxi licenses in New York City were traded on the secondary market for substantial sums (Kahn, 1988, Vol. II, p. 111; Fingleton *et al.*, 1998, p. 33, fn. 66).

[35] A good example of this is taxi regulation in Ireland. The Taxi Regulation Review Group (2011), based on the Indecon (2011) finding that there were between 13 and 22 per cent oversupply in the number of small public service vehicles (SPSVs), recommended a series of qualitative policy measures designed to improve compliance with existing regulations/rules and the quality of vehicles with the effect of reducing the number of SPSVs, the overwhelming proportion of which are taxis. However, there are grounds for arguing that the estimate of oversupply is too high (Gorecki, 2012b).

[36] The discussion in this paragraph is based on Gorecki (2009b, Table 2, p. 38; and Table 4, p. 42; 2011b). The capital values cited in the opening sentence are in €1999/2000, while the increase in the value of a taxi license in Dublin is in €1980. The airline price increases refer to the US and Ireland. In the case of Ireland, the estimate of 33 per cent is based on the real decline in the Dublin-London price, 1985-1995.

1986); cement, 67 years (1933-2000); public houses 110 years and still extant (1902 to present);[37] taxis 22 years (1978-2000); and, buses 80 years and still extant (1932 to present).[38] An exception is pharmacy restrictions on the location of new pharmacies which lasted only 6 years, from 1996 to 2002, because a High Court judgment caused the entry controls to be dropped by government.[39]

It could, of course, be argued that the transfer of income from consumers of these services through higher prices to the providers of the services is not a cost to society as a whole in terms of forgone output or inefficiency, but rather only a redistribution of income. Furthermore, some of these groups are, it could be claimed, in some sense deserving and so there is an element of social justice involved. However, these arguments do not stand up because direct regulation involves distortions and questionable allocations of resources. *First*, while many groups make active representations for direct regulation, not all such attempts are successful. Such rent seeking behaviour consumes resources that arguably have little social worth or output (Krueger, 1974; Posner, 1975; Tullock, 1967). *Second*, having obtained direct regulation, the incumbents seek to protect the benefits of such regulation from new entrants.[40] For example, in Ireland between 1996 and 2002, a public notice had to be given by a person intending to open a new pharmacy.[41] Existing pharmacies, whose profitability might be adversely impacted, were then given an opportunity to object and, if necessary, appeal to the Minister of Health to refuse the application. *Third*, the rents may be dissipated by those subject to direct regulation because of the lack of competition, leading to X-inefficiency and lack of innovation.

Fourth, entry and exit is an important channel of productivity growth.[42] Entrants are often the source of new ideas and innovations that challenge the status quo. Incumbents may be reluctant to invest in new technology that might render existing investment obsolete. By restricting entry through regulation, productivity growth is slowed.[43] *Fifth*, consumers experience not just higher prices because of

37 There was some relaxation in 2000. For details see OECD (2001, p. 204).

38 It should be noted that the discussion is centred on direct regulation that limits or places restriction on entry rather than regulation per se. In the case of taxis, for example, there are good reasons, based on market failure, for setting a maximum price and specifying certain quality standards, but not placing quantitative limits on the number of taxis. For further discussion see Fingleton *et al.* (1998).

39 Similarly quantitative limits on the number of taxis were found illegal in a 2000 High Court judgment (OECD, 2001, p. 207).

40 In other words, the current beneficiaries of direct regulation, especially if they have purchased a licence on the secondary market or used the value of the licence as a security against which to borrow, are likely to protect their privileged status from would be interlopers seeking to capture some of the rent.

41 This is discussed further in Gorecki (2011b, p. 522).

42 Baldwin and Gorecki (1991) and Scarpetta *et al.* (2002).

43 On the positive impact of the first five years of the single European aviation market, in terms of lower prices and greater choice see CAA (1998).

direct regulation on entry, but also enjoy less choice and possibly lower service quality. Waiting times for taxis increase (Goodbody, 2009, Table 6.3, p. 49), some geographic areas may be underserved by pubs (Competition Authority, 1998, pp. 36-50) or pharmacies (Competition Authority, 2001, pp. 12-13) due to entry restrictions. *Sixth*, persons and resources that are prepared to enter a sector and are denied access in a period of austerity when jobs are scarce. Unemployment may consequently be higher than it otherwise would be. *Seventh*, while the initial enterprises in a market are subject to direct regulation gain, if they subsequently sell their taxi or pub or pharmacy license, then the new owner will not earn any rent unless there are unanticipated price increases. This reflects the possibility that the regulation induces a future stream of excess returns that are then captured in the value of the license. Tullock (1975) referred to this as the transitional gains trap. This makes any subsequent reform, without compensation, difficult. *Eighth*, the evidence suggests that in many cases the alleged oversupply or destructive competition did not justify direct regulation.[44] *Ninth*, the evidence suggests that restrictive regulation is often very long lived and hence is likely to be difficult to reverse once things have improved. *Tenth*, the impact of the restrictive regulation extends beyond the regulated sector to the economy as a whole. Barone and Cingano (2011), drawing on evidence for OECD countries, find that the less the incidence of such regulation in the service sector (particularly professional services and energy regulation), the better the economic performance of the downstream manufacturing sector in terms of value added, productivity and export growth. This is redolent of the discussion in Sections 1 and 2.3 above that drew the distinction between the non-traded and traded sectors.

2.5 Competition and Regulatory Policy Intervention to Promote Greater Economic Security: Some Conclusions

The evidence suggests that providing economic security through relaxing competition and regulatory policy is costly. It creates two groups in society: insiders who benefit from increased security and outsiders who are not in receipt of such protection. While the insiders receive protection from market forces, the outsiders bear the cost in terms of increased prices, poorer service quality, higher unemployment and lower wages. In part this asymmetry is likely to be a reflection of the fact that the insiders (those that benefit from the relaxation of competition and regulatory law) are concentrated and well organised while the outsiders (those that bear the cost) are disparate and each person only bears a

[44] On pharmacy regulation in Ireland see Gorecki (2011b), on taxis in Canada see Economic Council of Canada (1981, p. 25), in Ireland see Fingleton *et al.* (1998), on trucking see Kahn (1988, Vol. II, pp. 178-185).

small cost.[45] However, even for the insiders there is evidence that in many cases the benefits are short-lived and accrue mostly to the initial group members subject to the greater economic security.[46]

Irrespective of whether or not the benefits are short-lived, providing increased security through relaxing competition and regulatory policy leads to longer term damage to the flexibility and success of the economy, which affects both the insiders and the outsiders.[47] This raises the issue of what ought to be the process for awarding greater economic security through competition and regulatory policy. Is there a framework that should be employed that might command greater and/or more deserved support?

3. Standards and Tests for Competition and Regulatory Policy Intervention

A corollary to the potential substantial adverse economic consequences of relaxing competition and regulatory policy is that such relaxation should be invoked only after careful consideration of the rationale for such relaxation as well as weighing the costs and the benefits. This further suggests relaxation is likely to be the exception rather than the rule. There are standards and tests contained within competition and regulatory policy and law that set out instances in which it is appropriate for otherwise anticompetitive agreements to be permitted and/or restrictive regulation to be introduced. In this section we briefly discuss the tests and standards that permit competition and regulation to be employed to supply a measure of economic security.

3.1 Competition Policy: Section 4 (5) of the Competition Act 2002.

Competition law contains provisions to permit what would otherwise be viewed as anticompetitive arrangements.[48] All agreements are subject to competition

[45] While the cost may be small in relation to an outsider's income or the gains of an insider, this does not mean that the outsider does not experience hardship. For example, if an outsider has to pay a higher price for a consumer durable, such as a car, or for an expensive pharmaceutical product that has to be taken for a prolonged period of time.

[46] This is consistent with the finding that direct regulation lasts for long periods of time while at the same time there is an active secondary market for licences to enter the regulated activity. Equally in the case of cartels that last, on average for close to a decade, a cartel member may be traded either as a private firm or alternatively its shares may be traded.

[47] It is no doubt for such reasons that the EU-IMF Programme for Financial Support for Ireland contains structural reforms that promote competition policy, liberalise the regulation of the legal profession and other measures designed to promote competitive markets. For details see EU and IMF (2010, 2011a, 2011b).

[48] In this discussion we concentrate on anticompetitive agreements. However, it should be noted that an abuse of a dominant position might be permitted if the same four conditions set out in the text in reference to agreements are met. (For a discussion see European Commission (2009)). An otherwise anticompetitive merger would be permitted if either: (i) the efficiencies flowing from the merger more than offset the anticompetitive price enhancing effects of the merger; or (ii) the acquired firm is a failing firm. In troubled times both of these defences might be expected to be

law, whether they are anticompetitive or not. However, where an arrangement is judged likely to breach competition law there are clear rules for when, despite this arrangement, it can be allowed. Broadly speaking the benefits of the arrangement should outweigh the costs.

Agreements that would otherwise be anticompetitive are allowed under competition law – at both the Irish (Section 4(5) of the Competition Act, 2002) and EU (Article 101(3) of the Treaty on the Functioning of the European Union) level – if four conditions are satisfied.[49] An agreement must:

- contribute to improving the production or distribution of goods or to promoting technical or economic progress,
- while allowing consumers a fair share of the resulting benefit.

But at the same time the agreement must not,

(a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; and,

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

The criteria balance the positive impact of the anticompetitive agreement against the possible price raising impact of the agreement, while at the same time ensuring that the distributional consequences are, in some sense, at least addressed. In contrast to a cartel, prices are less likely to increase. The test is a longstanding provision of both EU and Irish competition law, with extensive European Commission (2004) guidance. It is commonly accepted as an appropriate framework within which to evaluate otherwise anticompetitive agreements in terms of balancing the costs and benefits.

In the context of markets and sectors facing difficulties adjusting to adverse economic circumstances, the EU has allowed a limited number of otherwise

advanced by the merging parties. However, they are rarely successful due to the stringent requirements that need to be satisfied. (See, for example, the merger guidelines of the Competition Authority (2002), the Authority's Kerry/Breeo merger decision where the issue of efficiencies was explicitly considered (Competition Authority, 2008, Section 9), and the Musgrave/Superquinn merger decision where the issue of failing firm defence was considered (Competition Authority, 2011c, paragraphs 47 to 62)).

49 It should be noted that until 2002 in Ireland (and 2004 at the EU level) enterprises could notify agreements to the relevant competition agency, which would determine whether or not the agreement was anti-competitive and, if it was, whether the four conditions set out in the text were satisfied. Subsequent to 2002 (and 2004) firms have to self assess whether or not an otherwise anticompetitive agreement satisfied these conditions. The purpose of the switch was so that competition agencies could investigate and prosecute cartels, rather than wash clean linen in public.

anticompetitive agreements aimed at restructuring in synthetic fibres, petrochemicals and bricks.[50] In the case of bricks, for example, where there was substantial excess capacity, a structural decline in demand and large inventories of unsold bricks, producers in the Netherlands were allowed by the European Commission to reduce capacity in the 1990s, subject to some safeguards so as to ensure that in other respects the producers competed.[51] In Ireland a recent attempt to secure an agreement to rationalise over-capacity in beef processing failed.[52] In some cases representative bodies in Ireland have been successful in securing a commitment of a carve out from competition law, despite unsuccessfully arguing to the Competition Authority that the benefits of the agreement exceeded the costs and thus met the conditions set out in Section 4(5).[53,54] Such policy responses by the State undermine the effectiveness of competition policy and encourage enterprises and employees experiencing difficulty in troubled times to appeal directly to elected representatives to secure an exemption.[55]

3.2 Screening New Regulations: Regulatory Impact Analysis

The well-known market failure framework sets out grounds under which governments can intervene to provide economic security to participants in individual markets. There is no need to rehearse that literature here.[56] One of the grounds that is particularly relevant in troubled times is destructive competition, although it is a rationale that while often invoked (e.g., pharmacies, passenger

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50 For a discussion of these cases and the treatment of restructuring agreements by the EU, see Whish (2009, pp. 600-601). These cases date mostly from the 1980s and 1990s. Often the agreements allow orderly reduction in excess capacity. In synthetic fibres, for example, the agreement envisaged an 18 per cent reduction in capacity over three years. An examination of the European Commission's *Annual Reports on Competition Policy* for 2008 to 2010 shows that restructuring is very much tied in with State Aid, rather than exemptions based on Article 101 (3). Indeed, no examples of the latter were mentioned.

51 Whish (2009, p. 601) provides some details, the rest are taken from the relevant European Commission decision (*ibid*, p. 600, fn.277).

52 For details see Competition Authority (2011a, pp. 22-23). The agreement was found to be anticompetitive (by the European Court of Justice) and not satisfying all of the criteria set out in Article 101 (3) (by the trial judge). However, Beef Industry Development Society (BIDS) withdrew from the legal proceedings before a definitive view on the issue could be reached on whether or not the conditions under Article 101(3) could be satisfied.

53 For example, in the case of an anti-competitive agreement concerning voice over actors and advertising agencies, an attempt was made to argue to the Competition Authority that the agreement met the conditions set out in Section 4(5) of the Competition Act, 2002. The Authority disagreed that the required standard had been met, but the representative body for voice over actors continued to press the Government to agree to a carve out from competition law. This has not, as yet, been enacted. For details see Gorecki (2009a, pp. 222-223).

54 Although not a carve out in the above sense, the move to impose a Code of Practice for Grocery Goods Undertakings, is likely to shield food processors and primary producers from the full rigours of competition, despite a lack of evidence to support the Code. (For details see Gorecki, 2009c).

55 Under the terms of the EU-IMF Programme for Financial Support for Ireland, which runs until the end of 2013, it is unlikely any such exemptions will be granted. The July 2011 update of the programme states, "[R]equests for exemptions to the competition law framework will not be accepted unless they are consistent with the goals of the EU/IMF supported programme for Ireland and the needs of the Economy" (EU and IMF, 2011a, p. 29).

56 See, for example, Breyer (1982) and Kahn (1988). Markets fail for a variety of reasons: the presence of firms with market power, such as monopolies; externalities such as pollution and climate change; and, imperfect information leading to financial and health and safety regulation.

transport, etc.) does not usually stand up to critical scrutiny.[57] The issue thus becomes what mechanisms should be put in place in order to address requests for regulation so as to ensure that proper analysis is conducted and acted upon. Ideally, a carefully designed set of guidelines should set out when regulation is appropriate, based on the market failure framework, together with an institutional mechanism that ensures adherence to best practice. Such best practice guidance is developed by bodies such as the OECD by carefully studying and surveying the record of its member countries.[58] The key requirements are rigorous objective analysis, transparency and strong support from Ministers, backed by a dedicated unit, in order to ensure consistency and compliance with the programme.

In 2005 Ireland introduced such an instrument, Regulatory Impact Analysis (RIA), under which new regulations are, in principle, thoroughly evaluated. An RIA:

> … is an assessment of the likely effects of a proposed new regulation or regulatory change. It involves a detailed analysis to ascertain whether or not the proposed new regulation would have the desired impact. It helps identify the side effects and any hidden costs associated with regulation. RIA clarifies the desired outcomes of the proposed regulatory change. It also provides for consultation with stakeholders to ensure that their views and interests are understood during the regulatory process (Department of the Taoiseach, 2005, p. 3).

RIA was introduced following the OECD review of regulation in Ireland in 2001 (Goggin and Lauder, 2008, p.5).[59] The OECD (2001, pp. 108-109), which had drawn up best practice guidelines for regulatory reform and RIAs, was thus able to apply this body of knowledge in its recommendations for improving regulation in Ireland.

After some experimentation following the OECD report, involving piloting the RIA methodology with a small number of government departments, an RIA methodology was rolled out across all government departments and offices in

[57] See, for example the references in the previous footnote and, for a recent example in Ireland concerning pharmacies see Gorecki (2011b).

[58] In relation to Regulatory Impact Analysis (RIA) – discussed later in the section – see OCED (1997) for how such best practice based on member country's experience is derived.

[59] Ireland requested the in-depth regulatory review given the extensive experience of the OECD in advising governments on this issue. Other countries which had participated in such regulatory reviews prior to Ireland included the United States, Spain, Denmark and the Czech Republic.

Ireland in 2005.[60] RIA and the broader better regulation agenda[61] were administered centrally through the Better Regulation Unit (BRU), which was part of the Department of the Taoiseach, in accordance with best practice. The evidence suggests that the implementation and application of the RIA has not lived up to expectations. Goggin and Lauder (2008, p. 6), in a review of the first two to three years sponsored by BRU, reported the perception of external stakeholders that progress was "disappointing."[62] The OECD revisited the better regulation agenda in Ireland in 2010. Although some progress was noted,[63] concerns were expressed with respect to the role of BRU[64] as well as criticisms in the application of RIAs.[65] The OECD (2010, pp. 28-34) set out a series of key specific recommendations designed to improve not only RIAs but the regulatory agenda more generally.[66] In coming to these judgments the OECD was comparing Ireland to the best practice guidelines it has developed based on the record of what works well in other advanced industrialised countries.

At the present time the future of the RIA and the better regulation agenda is unclear. The BRU itself was abolished in 2011, with the staff assigned to other duties.[67] In February 2012 the government, although recognising the importance of robust and consistent RIAs, acknowledged that "... there is now a lacuna at the centre of Government as this responsibility has yet to be reassigned."[68] New "... structures to improve coordination and synchronisation"[69] are to be introduced by the end of 2012. One element of the new structure might be the recently announced Government Economic and Evaluation Service part of the mandate of

60 Goggin and Lauder (2008, p. 6). The methodology is set out in Department of the Taoiseach (2005).

61 For details, see, for example, Department of the Taoiseach (2002, 2004, 2009).

62 Goggin and Lauder (2008, p. 7) also comment, that in "… interviews, representatives of the business sector expressed strong criticism of the lack of visibility of RIAs; they felt that either they were not done, or, if done, many were not published, which meant opportunities for critiques of RIA by business or academics had not developed. Where RIAs had been done, there was a lack of credible consultation; and risk assumptions and estimates of costs and benefits had not been consulted on, and timescales in some cases unrealistic. The timing of RIAs was frequently criticised; they were seen as an 'add-on' which happened at the end of the regulatory process, rather than a fundamental part of it. The quality of published RIAs was considered poor …".

63 For example, the OECD (2010, p. 21) stated that "… BRU is an active advocate and promoter of RIA, and its activities have been met with some success."

64 The OECD (2010, p. 17) states that the BRU needed to be reinforced, "… not least in terms of securing supportive connections with the other parts of the Department of the Taoiseach." Furthermore, BRU "… lacks powers, and may be short on the necessary resources to do an effective job" (*ibid*, p. 17).

65 These criticisms include: "… the gap between the principles of RIA and the practice generally remains wide" (OECD, 2010, p. 22); "Currently there is not statutory backing for the RIA process." (*ibid*, p. 22); "The [RIA] process lacks sanctions and a strong challenger that would force departments to pay attention." (*ibid*, p. 22); "The analytical framework and quantitative support for RIAs remain relatively weak." (ibid, p. 22); and, "Significant statutory instruments (secondary regulations) may be slipping through the net." (*Ibid*, p. 23).

66 These included the "need to strengthen their [RIAs] quality", that "… draft proposals cannot be tabled before cabinet unless there is a RIA attached of adequate quality," and to see "… how publication [of RIAs] might be made a statutory requirement." (OECD, 2010, p. 31).

67 This is based on an answer to a Dail Question 11 October 2011. For details see http://debates.oireachtas.ie/dail/2011/10/11/00120.asp. Accessed 2 February 2012.

68 Department of Jobs, Enterprise and Innovation (DJEI) (2012, p. 37).

69 *Ibid*, p. 38.

which includes RIAs.[70] However, at this point the service appears to be more of a support function, rather than an overarching oversight, monitoring and compliance mechanism for government.

In sum, the process of putting in place a rigorous and effective system for evaluating new regulations has been ongoing for in excess of 10 years and remains incomplete. New structures and strengthened procedures are needed. As a result of the weaknesses and shortcomings in the current regime there can be no guarantee that new laws and regulations are being subjected to the prior scrutiny and analysis that they should be, with the result that the adverse consequences outlined in Section 2 are not being avoided. Of course, this may change by the end of 2012 depending on what new structures are put in place, but this is unlikely to be before 2013. The OECD (2010) sets out a clear roadmap of what is required.[71]

3.3 What Standards and Tests for Intervention?

Internationally there are well thought out and established tests for allowing otherwise anticompetitive agreements to be exempt from competition law and for approving regulatory proposals that might restrict competition. In both cases the test is one of whether the benefits exceed the costs, although the details – as noted above – vary as between competition law and regulatory practice. The approach adopted in Ireland in both cases is based on international best practice. However, in the case of *ex ante* review of regulation through RIAs a number of changes are still necessary in order to comply with international best practice. Policy announcements are expected by the end of 2012 on this issue. The very existence of these mechanisms no doubt prevents some anticompetitive agreements and restrictive regulatory proposals, where the benefits are less than the costs, from being proposed much less implemented.[72]

70 For details see Department of Public Expenditure and Reform (2012).

71 These requirements for the roadmap involve rectifying the problems identified in the OECD (2010) review referred to above. Hence, for example, consideration should be given: to "... increase the powers of the Better Regulation Unit" (*ibid,* p. 29); to check "Irish arrangements against those of relevant EU countries to see what might be done to strengthen the RIA requirements so as to strengthen their quality" (p. 31); and, to consider "... how to further boost methodological support and buy in departments for a quantitative approach" (p. 31).

72 In this context it should be noted that the Competition Authority has a role not only in relation to anticompetitive agreements, but also, under the Competition Act 2002, in advising government on the effects on competition of regulatory proposals. An examination of the Competition Authority (2012) Annual Report for 2011 demonstrates the breadth of regulatory proposals that the Authority has made representations concerning their impact on competition.

4. Conclusions

The purpose of this paper has been to address the issue of what role competition and regulatory policy should play in troubled economic times. Should these policies be: (i) relaxed to address concerns over economic security occasioned by the prolonged recession resulting in a series of austerity budgets; or (ii) enforced irrespective of the economic and budgetary conditions in which Ireland finds itself? In a small open economy such as Ireland's, it is important that markets are competitive and regulation that raises costs and inhibits the flow of resources between sectors should be avoided. Competition drives productivity growth which increases living standards and promotes competitiveness. Is this rationale still valid in abnormal economic times such as the present recession?

To address the issue of whether or not competition and regulatory policy should be relaxed to address concerns over economic security in troubled times the following questions were posed:

- What does the international as well as Irish evidence suggest is the economic effect of such relaxation?
- Does relaxation of competition and regulatory policy provide economic security? If so, at what price?
- Are there any conditions under which groups or sectors should be sheltered from market forces to provide greater economic security?

Competition policy can be relaxed through under-enforcement and permitting carve outs or exemptions from competition law. Regulatory policy can be relaxed through changing the mandate of existing regulators to weigh more heavily the welfare of the regulated entity as compared to consumers and to allow more direct regulation under which entry into a particular market is restricted. These mechanisms, by providing protection from competition, can provide a measure of stability and security for incumbent enterprises and their employees. Yet evidence from a wide variety of sources, time periods and jurisdictions suggests that the economic impact of such policies adversely impacts on growth, productivity and competitiveness.

At the level of an individual market, relaxing competition and regulatory policy leads to higher prices and less competitive pressure on enterprises to innovate and grow. The evidence suggests that the impact of relaxing competition and regulatory policy often lasts many years, making reversing these policies once the recession is ended challenging. At a wider economy level, there is less flexibility as resources cannot easily flow between different activities. The export or traded sector is damaged by having to pay higher input prices for goods and services produced in the non-traded sector, thus harming their competitiveness on international markets. The evidence suggests that relaxing competition and regulatory policy in a recession is likely to hold back the subsequent economic recovery.

Nevertheless, despite these adverse economic effects, if relaxing competition and regulatory policy results in increased economic security then this may provide offsetting benefits. Such relaxation involves a redistribution of income from consumers, including businesses (who pay higher prices) to the favoured group. However, such benefits are likely to be transitory, with the result that there will be continued pressure to raise prices. Furthermore, in many cases it is not clear that there is a valid rationale for the relaxation of competition and regulatory policy in terms of favouring a particular group.

Competition and regulatory policy do contain provisions that permit otherwise restrictive agreements and regulations to be allowed, but only when the benefits exceed the costs. These well established precedents are contained in Irish competition law, but the regulatory process in Ireland has, as yet, to fully reflect international best practice in judging *ex ante* regulation. The OECD (2010) report sets out the steps that need to be taken in this regard. By adhering to such a framework there is a clear and consistent basis on which decisions to provide economic security can be based; the alternative is *ad hocery* and temporary expedients, which encourage unproductive lobbying. Much better that effort should be concentrated within a framework that promotes sound analysis and careful evaluation of costs and benefits.

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