HOT AIR?

How antitrust watchdogs might help Europe hit its Green Deal goals

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HOW ANTITRUST WATCHDOGS MIGHT HELP EUROPE HIT ITS GREEN DEAL GOALS

The European Commission (EC) is currently consulting on the role of competition policy in helping to deliver the Green Deal. The consultation notes that "*competition policy is not in the lead when it comes to fighting climate change and protecting the environment"* and cautions that *"there are better, much more effective ways, such as regulation and taxation."* Nonetheless, it continues, "*competition policy … can complement regulation and the question is how it could do that most effectively.*"

The economic conundrum at the heart of climate change mitigation is a free-rider problem: the costs of mitigation are borne locally while the benefits are enjoyed globally. The economic theory of externalities shows that in such circumstances, the provision of measures to alleviate climate change will be insufficient. Similar issues arise with regard to other environmental concerns, such as river pollution, air quality, and so on.

Competition can in some cases make the challenge of dealing with environmental hazards even greater by driving firms to focus narrowly on the interests of the consumers they serve, even when these interests clash with those of wider society. A monopoly producer may be able to reduce polluting practices in response to pressure from lobby groups or politicians without having to worry about haemorrhaging sales (after all, its customers may have nowhere else to turn even if the new measures inconvenience them). Taking such steps may reduce the monopolist's profits somewhat, but it may still conclude that this is a small price to pay for avoiding the negative publicity (as the economist John Hicks once put it, "the best of all monopoly profits is a quiet life"). In a fiercely competitive market, however, the risk of losing business to rivals may make it impossible for even well-intentioned firms to make changes that its customers do not favour.

This is not to say that one should encourage a move to monopoly, as competition has many other benefits. Indeed where measures to promote environmental sustainability are popular with consumers themselves, competition can be a powerful driver for firms to adopt these measures. But it does point to at least a potential

EXEC SUMMARY

Europe's competition commissioner, Margrethe Vestager, has kickstarted a debate about whether competition policy should be doing more to help Europe hit its ambitious Green Deal target of making the continent carbon neutral by 2050. At first sight, competition and environmental policy may appear to be strange bedfellows: one has a laser-like focus on championing the consumer; the other has a brief to save the planet. What steps, if any, could Europe's antitrust watchdogs be taking to help the continent meet its sustainability objectives? And do proposals that have already been developed by some national competition authorities provide a template for the rest of Europe to follow?

tension between competition and beneficial societal outcomes which is not typically present.

The standard economic solution to such collective action problems is to effect coordination at a central level – whether through setting minimum standards, taxing environmentally detrimental activities or the outright banning of certain practices, materials or production methods. Typically, such measures are the responsibility of central government and hence outside the scope of competition policy. However, in principle they could also be implemented at industry level, in which case they would come under the competition umbrella. This could create some interesting tensions for the application of competition policy.

For instance, suppose a competitive industry is engaging in a polluting activity. This could be through generating carbon emissions, using non-biodegradable plastic, putting particulates into the air, and so on. The owners/managers of those individual firms may want to scale back their harmful practices. But to do so would increase their costs and thus damage their competitive position, making such a course of action unprofitable.

The owners/managers of the firms concerned could respond by coming to an agreement with rivals to change their production processes to reduce pollution (but would otherwise continue to compete independently). The outcome would be less pollution but higher prices for consumers. Under the classic competition policy approach, regulators would take the view that in a situation like this it is not for the firms to decide whether it is best for consumers to pay more for a greener product. That is the role of central government. The firms in question would therefore likely be found to have breached Article 101 of the Treaty on the Functioning of the EU (TFEU) or equivalent provisions prohibiting agreements that disrupt free competition.

DIFFICULT QUESTIONS

Potentially, it could be argued that there is an objective justification for such agreements, in that the benefits of cutting pollution outweigh the higher costs. But as things currently stand, it is not clear whether or how competition authorities should recognise those benefits as being relevant. Such an expansion of competition law requires a practical framework which is accepted by all parties. But when one starts thinking about potential frameworks, a few interesting questions arise.

- **First, what would count as a "sustainability" agreement that might be considered for exemption from Article 101 TFEU**? Reducing carbon emissions is one thing, but why stop at decarbonisation – or even the environment? After all, there is a plethora of collective action challenges that could be undermined by the dynamics of market competition. For example, in June 2020 a report by the Fairtrade Foundation on "competition law and sustainability" argued that competition law was deterring retailers from collaborating to tackle low incomes and wages in the supply chain. The basic collective action problem was the same as that described above for environmental issues: competition between suppliers was forcing a race to the bottom on costs that ignored wider societal objectives. But the broader goals that the report said should be taken into consideration by competition authorities were of a different nature.
- This points to a second, broader question: what should an antitrust regulator's **guiding mission statement** be on whether the benefits of a sustainability agreement justify the cost? Should the EC focus solely on the welfare of European consumers or should it also place weight on benefits that

accrue to people elsewhere in the world? Should it focus on the interests of consumers who are alive today or should it place equal weight on the interests of future generations? And what should it do when different sustainability objectives rub up against one another? For example, an agreement between supermarkets to source their food locally in Europe might reduce carbon emissions from transport, but it may also be harmful for low-income farmers in developing countries. Triangulating these competing goals requires difficult value judgments that have traditionally been the purview of elected politicians, not regulators.

- Setting aside these conceptual issues, there is a third question as to how competition authorities should go about **measuring these costs and benefits in practice**. Suppose the benefits relate to reduced air pollution. The evidence suggests that cutting air pollution is likely to result in better respiratory health, but how should a monetary value be placed on that outcome? In the UK, the National Institute for Health and Care Excellence (NICE) uses the concept of QALYs – quality-adjusted life years – to evaluate whether specific health interventions are worth carrying out; a QALY is typically judged to be worth £20,000 to £30,000. While in principle this methodology could be used to assess pollution mitigation agreements, this is evidently a complex exercise and is likely to be difficult for parties to carry out and for competition authorities to appraise.

  Greater challenges are likely to arise where the environmental benefits are less clearly linked to health outcomes or where the method for estimating the monetary value is still evolving. Take, for instance, an industry seeking changes to production processes that cause microplastics to run off into the water system and ultimately into food that we eat. There is concern that ingesting microplastics can affect human health, but the evidence base is still being developed. Without a clear way of measuring the damage, it will be hard to make a compelling case to a competition authority for the benefits of reducing microplastics, regardless of worries about their impact on marine life.

Such complications would add to the practical challenges businesses face when trying to persuade competition authorities to allow them to enter into agreements with one another on the basis that they promote technical or economic progress. While such a provision exists in European competition law under the so-called Article 101(3) exemption, in practice the bar for persuading the Commission to permit an arrangement on these grounds is set very high. Companies have to demonstrate not only that the benefit to consumers outweighs any costs arising from a loss of competition, but also that the proposed agreement is indispensable to the attainment of these objectives. Tellingly, a 2019 study published by the University of Leeds found that businesses sought to invoke Article 101(3) on 45 occasions during EC investigations between 2004 and 2017, but on no occasion was it accepted by the Commission as a justification for anti-competitive conduct.

DUTCH COURAGE

Despite these hurdles, some European countries have already taken steps to build sustainability considerations into their antitrust regimes. In the vanguard is the Dutch Authority for Consumers and Markets (ACM), which has published draft guidelines on “sustainability agreement” exemptions from Article 101 TFEU. So how has the ACM addressed the challenges described above?

Starting with the first issue, the ACM does not propose to provide “a comprehensive or precise definition of the term sustainability”. Rather it intends to adopt the UN’s definition, namely any development towards “an economically, socially and environmentally sustainable future for our planet and for present and future generations”. This appears to allow room for a broad range of issues to be considered under the heading of sustainability, including not only climate change, pollution and biodiversity, but also fair trade and socio-economic development.

This point is reinforced later in the guidelines, with the ACM explicitly stating that it will consider both “environmental damage” and “other sustainability” agreements. The former are “agreements that aim to improve production processes that cause harm to humans, the environment, and nature” and should contribute to environmental standards or goals that the Netherlands has signed up to, nationally or internationally. The specificities of “other sustainability” agreements, by contrast, are not defined.

Nor has the ACM provided guidance on the other questions raised above:

- On the matter of how to quantify the benefit of sustainability agreements, the ACM suggests that in at least some circumstances, businesses may not have to quantify them at all. Companies, it suggests, can submit a “qualitative analysis” instead of a quantitative one when the harm is “obviously smaller than the benefits from the agreement”. However, it is not clear how common such “obvious” cases would be in practice: the ACM provides an example of an agreement where risks to competition may be low because the need for coordination is temporary and/or involves a minor input in the production process, and results in a beneficial outcome that many consumers themselves sympathise with. However, in these circumstances it may be harder to demonstrate that coordination between businesses is essential for delivering the sustainability benefit in the first place. After all, if an environmentally friendly action is popular with many customers, companies may want to be seen to be the first movers, stealing a march on their competitors.

- Nor is it obvious to us how the ACM will assess any cases where the trade-off between sustainability benefits and costs to competition is more ambiguous. The ACM is clear that it will not restrict its assessment to ‘paying’ customers when thinking about costs and benefits. In other words, the ACM could wave through a sustainability agreement even if it leaves consumers who buy the products or services in question worse off. However, it is yet to be seen how widely the ACM will be willing to cast the net when assessing this broader benefit. Will it consider only the interests of those living in the Netherlands or will it place equal weight on the interests of people across Europe or the globe? And what about environmental benefits that accrue to animals or the natural world rather than directly to humans?

The breadth of the ACM’s guidance may give companies scope to think creatively about agreements that can promote sustainability. It may also give the ACM leeway to consider new sustainability issues that might arise in the future. By the same token, however, this approach provides scant guidance for businesses as to what evidence to present to the ACM, how to frame their arguments or what their chances of prevailing will be.

Some other national competition authorities have also begun to grapple with these challenges. For example, Greece’s Hellenic Competition Commission has published a staff discussion paper in which it recognises that sustainability considerations may require it to adopt fundamentally different frameworks to the “price-based revealed preference” model that underpins the approaches that competition authorities currently use to measure consumer welfare. In particular, given that sustainability agreements are by their very nature likely to weigh up costs and benefits that extend far into the future, regulators may need to consider intergenerational models that take into account the welfare not only of today's consumers but also of those not yet been born. Some other regulators may already have valuable insights into how to take the interests of future generations into account when deciding what costs it is acceptable to impose on current consumers. In the UK, for example, the energy regulator Ofgem has a long-established statutory duty to take the needs of "current *and* future consumers" into account in its decision-making. It is not clear whether antitrust watchdogs will look to consult these regulators or other bodies experienced in applying the relevant analytical frameworks and techniques, or whether they will seek to develop this expertise themselves.

TOO HOT TO HANDLE?

In light of these complexities, competition authorities may be tempted to conclude that taking on climate change and other sustainability challenges is a matter not for them but for central government. That would make sense if one took the view that governments operate perfectly with full information and no legislative or other capacity constraints, so that whenever a sensible regulation can be developed, it will be introduced in a timely fashion.

However, it is not obvious that the assumption of perfect government holds, particularly at present: governments across the world are too busy handling the Covid-19 pandemic to pay much attention to less urgent matters. In the UK in particular, and to a lesser extent the rest of Europe, the effects of Brexit are another time-consuming preoccupation. And while it is for governments to set the direction of policy, the involvement of regulators – with their specialist expertise and day-to-day experience of interacting with businesses – is often vital in ensuring these policies survive contact with reality.

A better way forward may be an approach whereby central governments and different regulators work together towards the goal of achieving more sustainable markets. Elected policymakers must take the first step in providing more clarity on the goals that society should be looking to achieve in balancing the interests of consumers against countervailing sustainability considerations. But these goals must then be translated into a concrete and transparent regulatory framework that provides businesses with clarity as to how their initiatives will be assessed in practice. And it is in designing and applying this framework where the experience of competition authorities can come to the fore. Competition authorities can already bring valuable expertise to the table in quantifying the costs of sustainability initiatives to consumers. And they may be able to draw on other regulatory bodies to provide clarity on how the countervailing benefits of a proposed agreement will be measured. Of course, such coordination takes effort, but any other approach may prove… well, unsustainable.

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