

PASCN Discussion Paper No. 2000-10

**Government Policies and Regulations:
Interrelationship with
Competition Policy Objectives**

Erlinda M. Medalla



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Erlinda M. Medalla

Philippine Institute for Development Studies

January 2000

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ABSTRACT

The paper aims to examine the major government policies in terms of how they relate to the objectives of competition; clarify what important trade-offs may exist; and determine how and possibly when conflicts between government policies and competition policy objectives arise. Three sets of government policies were discussed. The first is trade policy, in particular trade liberalization, where the impact on competition is most direct and apparent. The second group covers government policies and regulations that have direct impact on competition, namely: 1) government regulation of an industry, or a segment of it; 2) direct government equity participation; and 3) other regulatory restrictions. The third group of policies consists of other major government policies with other development objectives and their interface with competition policy objectives. These include industrial policies, agricultural policies and environmental policy and regulations. In general, the paper points out the need to bring in more closely the principles of competition policy into analyzing and evaluating government policies. Indeed, competition policy would provide a new and different perspective that could help formulate a more effective and dynamic development policy for the Philippines.

Government Policies and Regulations: Interrelationship with Competition Policy Objectives

Executive Summary

Almost anything the government does could have an impact on competition and competition policy objectives. Although, competition is not the goal in itself, its role in improving efficiency and allocating efficient resources make it a key element in the government's pursuit of economic and social objectives. And if some government policy runs contrary to competition principles and guidelines, there is enough basis to at least re-examine this policy. Evaluating policies in the light of competition policy objectives does not imply prioritizing competition and efficiency objectives over others. It would only make more transparent the trade-offs and the decision making process.

The paper examined three sets of government policies in terms of how they relate to the objectives of competition. The first is trade policy where the impact on competition has been thus far most significant and apparent. The second covers government regulations which have direct impact on competition. In general these include:

- Government regulation of an industry, or a section of it,
- Direct government equity participation, and
- Other regulatory restrictions.

The third set deals with the other major government policies with other development objectives but nonetheless have significant interface with competition policy. In particular, this includes:

- Industrial policies
- Agricultural Policies
- Environmental policy and regulations.

The last would also have direct restrictive effects on competition but is considered here because of other objectives which are paramount to it. Finally, the paper provides the summary and conclusions.

With respect to the first, trade liberalization could represent the first major layer of competition policies to be implemented. Where there are no natural barriers to trade and the good is tradable, trade liberalization would clearly enhance competition, at least by making the market more contestable.

To be sure, even if trade were liberalized by removing or lowering both tariff and non-tariff barriers, there are still other factors to consider to assess how much competition results. Most important to examine is the structure of the local distribution channels. If the local distribution channels are somehow tied up with local producers (e. g., through vertical integration or some vertical agreement like exclusive dealing), then the impact of trade liberalization may be limited (especially if substantial sunk costs are involved in putting up another distribution channel).

Also, although trade reforms during the past decade or so have substantially removed or reduced tariffs and import controls, there are still some important barriers to trade that remain. Moreover, more recently, newer forms of protectionism are

becoming more important-- anti-dumping measures and possibly to a lesser extent, the subsidies and countervailing duties.

With respect to the second set of policies, in general, the government would have reason to intervene in cases of market failure. Among the most important and most recognized of these are (1) the presence of economies of scale and (2) externalities. The intent of these regulations are in fact, basically pro-competitive. That is, since the market, in such cases of market failure, would not be able to in achieve efficiency if left to itself, and some regulation is needed to assist it to do so. Thus, a regulatory framework may be called for.

The foremost examples of such cases are considered to include: the Energy Regulatory Board (ERB) for electricity and the National Telecommunications Commission (NTC) for the telecommunications industry, The Philippine Ports Authority (PPA) and the Maritime Industry Authority (MARINA) for the shipping industry, the Civil Aeronautics Board (CAB) for civil aviation industry and the Central Bank for banking.

Although regulations may be justified, considering the power that the regulator has, and the (monopoly) rights given the firm allowed entry, a careful review is necessary with respect to what is the real impact of the regulation. The paper points out the relevant issues that need to be looked into.

First is a tendency for the regulation to cover a greater portion of the industry than necessary and for the regulator to "over-regulate." How much of the industry could be deregulated, and/or how much of the regulation can be relaxed? Are there elements/activities in the industry covered by the regulation which should be made subject to competition? Indeed, especially after the era of controls under the Marcos regime, there was increased realization of these costs of regulation which spurred the policy thrust towards deregulation in all these industries. The benefits of deregulation are still being felt -- in shipping, domestic air travel, and telecommunications in particular. Nonetheless, a lot more could probably still be done. Specifically, clearer delineation between segments (activities) in the industry which are natural monopolies and those which should be subject to more competition must be made. Related to this is, how "essential" is the essential facility? Is there a clear policy access to essential facility. The third question is the policy of cross-subsidization. There is a need to re-evaluate the costs and benefits of cross-subsidization. Fourth, a problem common to all regulations is that the regulator could become subject to "capture." What safeguards need to be put in place? Finally, another problem, also common to all regulations, is the tendency to use complicated and cumbersome procedures which could negate whatever pro-competitive effects there could be. Regular review to update and streamline the procedures would go a long way to increasing the efficiency of the regulatory process and the industry itself.

With regards to direct government equity participation, the problem may not be whether or not to transfer ownership but rather how the competition process and discipline could be introduced. If there would be transfer of ownership, all unnecessary advantages previously enjoyed by the firm should be removed and competitive neutrality should be ensured.

On other regulatory restrictions, these could range from explicit restraints to entry requiring firms to obtain permit or license to operate in a particular market to stringent procedural and other requirements making entry to a market difficult. These include among others: a) Local Government Code provisions on licensing and zoning; b) Lengthy and cumbersome bankruptcy and insolvency laws forming exit barriers; c) Labor Code provisions which restrict flexibility of firms to downsize or shut down also forming exit barriers; d) Intellectual property rights protection; e) Government procurement policy; and f) Business registration requirements.

With respect to the third set of policies, although intended to serve other explicit objectives, the question is how much should competition policy be considered in the formulation of these policies?

For the investment policy as a whole, the objective is to aid in industrial growth and development. The thinking behind this is that there are market failures which prevent the industrial sector from developing naturally. Indeed, there is greater conscious consideration of this rationale for role of investment policy. This is reflected in the shortening of the list of industries in the Investment Priorities Plan (IPP), and moving towards a more promotional body. The "measured capacity" concept in the Omnibus Investment Code which limits granting of incentives when a certain capacity (some optimum scale) is reached, clearly anti-competition in nature, is not followed in practice. There is a move towards the "greening" of incentives, realizing externalities involved. Export promotion remains in the list of priority. As noted above, regional dispersal of industries and promotion of regional investment have been among the stated goals of the Philippine government.

These are arguably desirable objectives. Nonetheless, an obvious strategy which has been overlooked is to proactively support competition policy for industry, since their objectives in a large part actually merge. Indeed, could competition policy actually serve as one of policy tool for industrial development (together with trade, fiscal and monetary policies)? Or, on the contrary, are there anti-competition effects which unintentionally go against the competition policy objective (serving to defeat their purpose)? One that comes to mind is the inherent bias of an incentive granting system against the entry of small and medium scale industries.

Of particular importance is the policy on foreign direct investment. Restrictions on foreign equity have a direct impact on entry of firms. Recently, some liberalization was implemented in retail trade with the passing of the Retail Trade Act. This could prove to have a big impact on competition. It would also compliment well the effects of trade reforms.

With respect to agricultural policy, a basic rule should also be for government to intervene only when market fails. However, for agricultural policies, there appears to be the additional, equally important (possibly more so in some cases), equity objective. This is where it could run counter to competition policy objectives. Nonetheless, if such trade offs exist, are they justified? That is, would benefits (from equity considerations for example) outweigh costs (e. g. efficiency losses from foregoing competition objectives).

In particular, agricultural policy still relies on tariff policy tools and other trade controls (anti-competition). Agricultural policies also employ government regulations with direct impact on competition. This include for example, the regulations implemented by the National Food Authority (NFA) and Sugar Regulatory Administration (SRA). These policies supposedly exist to protect income of farmers (equity objective). Are the costs of protection and regulation commensurate to the benefits of increased income for the farmer? These are important questions to ask.

With respect to environmental policies, environmental concerns are usually characterized by externalities. This means that environmental policy and management would need measures to internalize these external costs and benefits. Where market-based instruments could be used, uniformly and fairly applied, no serious impediments to competition are expected. However, in many cases, regulatory (command and control measures) are usually the more expedient tools--from standard setting to permitting requirements. Examples are the environmental impact assessment (EIA), environmental clearance certificate (ECC) required for a number of industries even before they can begin to operate. Some industries also complain about the impact on competitiveness of such legislations as the Clean Air Act. They could restrict entry and/or entail prohibitions, most especially affecting small and medium scale industries. Again, there are trade-offs. And the question is would benefit (from environmental regulation) outweigh the costs?

In sum, what all these indicate is the important interface between these policies and competition policy. And what is implied is a need to closely re-examine these government policies in the light of competition objectives. Again, competition is not the end in itself. Rather, the objective is to clarify what kind of trade-offs exists and to make them transparent so that judicious decisions could be made and reforms implemented if called for.

In general, the paper points out the need to bring in more closely the principles of competition policy into analyzing and evaluating government policies. This is especially true in the pursuance of needed reforms in government regulations. Recognizing its role in the major government policies will shed more light into how effective these policies are. Indeed, competition policy would provide a new and different perspective which could help formulate a more effective and dynamic development policy for the Philippines.

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Government Policies and Regulations: Interrelationship with Competition Policy Objectives

*Erlinda M. Medalla**

1. Introduction

Conceivably, almost anything (and everything) the government does, could affect competition. There may not be any conscious, coherent, or concerted policy on competition, but government policy interventions will nonetheless always alter, in varying degrees, for good or bad, the state of competition. It is thus ironic that for a developing country with usually less perfect markets, there is a greater need for an effective competition policy to encourage better use of scarce resources but less recognition of this need.

This is, however, not difficult to understand. Implementing competition policies is a formidable task even for a developed country. For developing countries like the Philippines, the difficulties are magnified many times over. Not only are markets less developed, tending to be less perfect, there are also many other more urgent social (often conflicting) objectives that need to be addressed. The government, hard pressed to find ways to hasten economic development and at the same time provide much needed social services, often would tend to adopt more interventionist policies and measures without enough consideration of the impact on competition.

Not that the government has done nothing to foster competition. The reforms starting in the mid-1980s have done much to move the economy towards a more competitive and market-friendly policy environment. Trade reforms, banking reforms, foreign investment policy reforms, deregulation, privatization, and the policy thrusts in general, during the past decade have explicitly and implicitly recognized the benefits from competition.

But it has done so many other things besides that may have to be re-examined in the light of competition policy objectives. There is a need to take a more comprehensive look at competition policy, covering not just the core competition policy of enforcing a rational anti-trust law, but the interrelationships between competition policy and the other government regulations and policies as well.

This is not because safeguarding competition and the competitive process should be the overriding objective. Rather, this is because, in general, there are efficiency gains expected from encouraging competition which should lead to economic growth and improved consumer welfare. And if some government policy conflicts with competition policy, there is enough reason to question if this policy serves national welfare on the whole and its stated objective in particular.

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Thus, this paper attempts to examine the major government policies in terms of how they relate to the objectives of competition policy. The aim is not to make definitive assessment and conclusions about the overall merits of these policies *vis-a-vis* competition policy. Rather, the objective of this paper is more to discuss what important trade-offs may exist and clarify the possible interface with competition policy. It aims to examine how and possibly when conflicts between government policies and competition policy objectives could arise. The paper does not promise to be exhaustive either. Instead, it would attempt to be more comprehensive by looking at the major policies and some typical policies that could have similar effects as others.

The paper starts in Section 2 with a brief discussion of the objectives of competition policy to provide a reference for discussion of its interface with other government policies. Then, the paper proceeds with the review of government policies by looking first at trade policy where the impact on competition is most direct and apparent. This is done in the Section 3. To organize the discussion further, the paper then groups the other government policies under two general headings. Section 4 deals with the first group which covers government policies and regulations which have direct impact on competition. In general these include:

- Government regulation of an industry, or a section of it,
- Direct government equity participation, and
- Other regulatory restrictions.

Section 5 then examines the second group of policies -- mainly the other major government policies with other development objectives -- and their interface with competition policy objectives. In particular, the paper has selected the following policies which affect the major sectors of the economy. This includes:

- Industrial policies
- Agricultural Policies
- Environmental policy and regulations.

The last would also have direct restrictive effects on competition but is considered here because of other objectives which are paramount to it. Finally, Section 5 provides the summary and conclusions.

2. Underlying Concepts and Objectives of Competition Policy

Competition is "a situation in a market in which firms or sellers independently strive for the patronage of buyers in order to achieve a particular business objective, e. g., profits, sales and/or market share. Competition in this context is often equated with rivalry. Competitive rivalry between firms can occur when there are two firms or many firms. This rivalry may take place in terms of price, quality, service or combinations of these and other factors which customers may value." (World Bank and OECD, 1999)

Such a competitive situation may also be effected by "market contestability." That is, competition comes not only from actual firms or sellers already in the market

but also from firms or sellers that could enter the market. In other words, the threat of entry is enough to provide competition and to make the market contestable. Monopolists and oligopolists would behave like "perfect" competitors when faced with the threat of new entrants into the market. (Baumol and Willig, 1981)

In the process, competition thus disciplines and regulates the market. In general, it is an efficient regulator, helping to allocate resources efficiently and maximize consumer welfare. It promotes efficiency not only in terms of producing more with less (technical efficiency) but also in terms of inducing better resource allocation (allocative efficiency). Allocative efficiency in a competitive setting is encouraged because producers and investors receive the correct market price signals which induce them to invest where there are highest returns. Indeed, the presence of competition is almost synonymous with an efficient functioning of markets. The end result is increased overall welfare reflected in wider consumer choices, lower prices and better quality of products. But perhaps even more important are the dynamic gains from innovation that competition fosters and the flexibility that it develops, on the whole enabling the economy to cope better with the ever changing environment

Desirable though its effects may be, the presence of competition is not always assured. There may be inherent structural factors and tendencies in firm behavior which would cause deviations from competition. At the same time, neither is it an end in itself, as there are times when the market could fail and competition would not lead to efficient resource allocation.¹ Thus, ideally, the government should promote competition when it fulfills its role as an effective regulator, and step in when it does not.

This, in essence, is what competition policy is about. The primary objective is efficiency. That is, competition policy should promote competition as long as it encourages efficiency and growth. At the same time, it should allow for seemingly anti-competitive set-ups and economic regulation where the market fails. In addition, if possible, competition policy should also be made consistent with social objectives. And ultimately, the goal is to increase welfare.

It could also be true in that competition policy would not only lead to increased efficiency but contribute to other social objective as well, e. g. equity. This arises from the fact that competition leads to a reduction in the economic power of firms and the greater majority represented by consumers benefit from lower prices, better quality and wider choices of products. Thus, no trade-offs or conflicts arise. There is thus even magnification of benefits from competition and this is well and good.

3. Philippine Trade Policy and Competition

The Philippine trade policy regime has changed substantially during the past two decades-- from a highly restrictive and protectionist system to a relatively open trade regime. Tariffs went down across sectors from highs of 100 percent (or even

¹This is elaborated on in the overview paper by the author, in this PASCN series on competition policy studies.

more) before 1980 (i. e., before the first Tariff Reform Program) to a present range of 3 to 10 percent for the majority of products. Tariffs of more than 30 percent are found mainly in agricultural products (e. g. sugar, rice, corn, livestock not for breeding, etc) and only in a few industrial products (e. g. completely-built-up cars). Non-tariff import restrictions, mainly in the form of import licensing requirements or outright import prohibitions have also been removed except for a few (less than 3 percent of commodities at the 6-digit level of classification). There are a few remaining import restrictions, again for some (basically the same) agricultural products and for reasons of health, sanitary and national security.

These reforms of the Philippine trade policy have been well-chronicled and well-studied and would not be further elaborated on in this paper. Suffice it to say that the series of trade reforms undertaken is largely due to the recognition of the huge costs of the three decades of protection and expected benefits from competition.

Trade liberalization and competition

Trade liberalization could represent the first major layer of competition policies to be implemented. Where there are no natural barriers to trade and the good is tradable, trade liberalization would clearly enhance competition, at least by making the market more contestable. The world market is a potential source of supply, so that even a monopolistic or an oligopolistic domestic producer, faced with threats of entry of competing imported goods, would act like perfect (or something less perfect but close) competitors.

To be sure, even if trade were liberalized by removing or lowering both tariff and non-tariff barriers, there are still other factors to consider to assess how much competition results. The World Bank/OECD study identifies the following factors:

- The existence of cross-border distribution systems,
- The amount of information that domestic buyers have about foreign firms,
- Whether foreign suppliers have been placed on approved sourcing lists,
- The existence of significant excess capacity held by foreign firms,
- The similarity between the needs of domestic buyers and needs of foreign firms,
- Exchange rate trends,
- The existence of technology licensing agreements, strategic alliances, or other affiliations between domestic buyers and foreign firms.

However, advances in information technology and declining transport costs across borders (especially relative to domestic transport costs) diminish the impact of these factors, with the exception perhaps of the third and the last factors. Indeed, if these concerns would have some impact on the ability of foreign products to compete with local supply, they may even enhance, not diminish, the competitive edge of foreign products over domestic supply because of some perceived (real or not) superiority of imported goods (i. e., like it or not, the presence of so-called colonial mentality of many local buyers).

What is more important to examine is the structure of the local distribution channels (the third and the last factors cited above are related to this). If the local

distribution channels are somehow tied up with local producers (e. g., through vertical integration or some vertical agreement like exclusive dealing), then the impact of trade liberalization may be limited (especially if substantial sunk costs are involved in putting up another distribution channel).²

Perhaps another consideration is that local firms could (and most likely do) resort to product differentiation. However, this would only offer minimal market power as foreign competition could potentially offer so much more. And if product differentiation leads to overall increased supply of goods, the impact is pro-competitive, resulting in a wider range of products and higher consumer welfare.

With these considerations in mind, the conclusion is that in general, where the good is tradable, and a close import substitute can freely come in, the market generally becomes contestable.³ The Philippines, being a small country is a price taker with respect to tradable goods. In this sense, trade policy has probably the most sweeping impact on competition.

Anti-dumping and countervailing measures

Although trade reforms during the past decade or so have substantially removed or reduced tariffs and import controls, there are still some important barriers to trade that remain. Moreover, more recently, newer forms of protectionism are becoming more important -- anti-dumping measures and possibly to a lesser extent, the subsidies and countervailing duties.

Theoretically, the anti-dumping act and the subsidies and countervailing act could be considered as competition policies being carried out at a global level. They are allowed under GATT-WTO codes to deal with "unfair" trade practices causing trade distortions that could hamper the efficient global allocation of resources. The intention is to prevent predatory pricing (dumping price) and unfair trade practices (subsidies giving exporting firm "unfair" competitive advantage) with these acts.

The problem is how close to the spirit of the code would the cases filed be in most instances? How prone are these provisions to being used as simply protectionist tools? As much as possible, GATT-WTO codes on anti-dumping and countervailing duties have tried to make rules transparent and predictable. However, it would still be the national laws on anti-dumping and countervailing duties which would be effective. Improvements in the Philippine national laws were made to make it more consistent with WTO rules.

Nonetheless, even with the perfect rules, in the end, it is the actual implementation and administration that would matter. If cases could be easily filed and authorities easy to find prima facie evidence, the mere threat of filing a case

²This is a problem, for example, in the case of the downstream oil industry. This is discussed in greater detail in a separate paper by Peter Lee U in this PASCN series of studies on competition policy.

³This was manifested even during the era of high tariffs when domestic firms would strongly oppose tariff cuts because they feel they would suffer significant reduction in market share. (Power, Bautista and Associates 1979).

would be an effective barrier to entry, whether the case is real or not. The number of cases being filed has been growing since the 1990s (See Table 1) and although still few in number, the anti-dumping act could be an effective tool of protection and a real barrier to trade. A lot depends on the orientation and objectives of the relevant authorities tasked to implement them.

Table 1
ANTI-DUMPING CASES, 1985-1995

| Year | Total No. of Cases Originally Filed | No. of Cases Dismissed | No. of Cases Imposed AD Duty | Articles Imposed AD Duty | Country of Origin |
|------|-------------------------------------|------------------------|------------------------------|---|-----------------------|
| 1985 | 2 | 2 | 0 | --- | --- |
| 1986 | 3 | 3 | 0 | --- | --- |
| 1987 | 6 | 6 ^{a/} | 0 | --- | --- |
| 1988 | 5 | 5 | 0 | --- | --- |
| 1989 | 1 | 1 | 0 | --- | --- |
| 1990 | 4 | 3 | 1 | Refraction Bricks | Thailand |
| 1991 | 6 | 4 | 2 | Refraction Bricks Safety Matches | Thailand Indonesia |
| 1992 | 0 | 0 | 0 | --- | --- |
| 1993 | 1 | 0 | 1 | Galvanized Malleables Coated Fittings | PROC |
| 1994 | 9 ^{b/} | 5 | 2 | Refraction Bricks PVC Resin | Thailand Korea |
| 1995 | 3 ^{c/} | 1 | 0 | --- | --- |

^{a/} includes 1 case withdrawn

^{b/} 2 cases pending with DOF

^{c/} 2 cases pending with DOF

Source: Medalla, Erlinda. 1996. "New Instruments of Protection"

The following section deals with other government policies and regulations with direct impact on competition and more closely related to competition policy objectives.

4. Government Policies and Regulations and Competition Policy

This section discusses government policies and regulations with direct impact on competition. They are direct government interventions which control either entry into the market or some aspects of operation in the market, or both. In general these include:

- Government regulation of an industry, or a segment of it,
- Direct government equity participation, and
- Other regulatory restrictions.

4.1 Industry specific regulations

No government measure and action could have a more direct impact on competition than attempts of the government to directly regulate an industry. And such strong involvement should also require a strong rationale.

In general, the government would have reason to intervene in cases of market failure. Among the most important and most recognized of these are (1) the presence of economies of scale and (2) externalities. The intent of these regulations are in fact, basically pro-competitive. That is, since the market, in such cases of market failure, would not be able to achieve efficiency if left to itself, and some regulation is needed to assist it to do so. Thus, a regulatory framework may be called for. Such regulation should aid the market in realizing optimum levels of output.

a. Economies of scale, natural monopolies and industry regulation

Economies of scale can arise from efficiencies in production which could only be realized upon the attainment of a certain plant size. Economies could also come from other stages or areas such as purchasing, marketing, and R&D activities. Such gain in efficiency from economies of scale, however, is not by itself an argument for regulating the industry and limiting the number of firms in the market.

Where the good is tradable

This is especially true where the good is tradable. If such a good with economies of scale is tradable, then it could also possibly have export potential and economies of scale need not be derived from serving the domestic market alone. If there are private initiatives to enter the market even without any promotion and

incentives from government, they could have very well realized the potential gains and entry into it should not be restricted and should even be welcome.

The problem is that the promise of economies of scale is a lure for governments to intervene, especially when the industry is also considered "strategic." The reasoning is that an initial push is necessary for private sector to see and act on this potential. Indeed, this appears to have been the strategy by the government during its protectionist and import-substituting phase. This has been the main reason, for example, in the local content program, promotion of steel, cement, and other heavy industries by the government during that time (and remains to be so in some cases). Generous incentives are granted to selected industries but at the same time, some regulations are also imposed. There have also been cases of direct government equity participation (e. g. National Steel Corporation).

As experience has shown, however, such a strategy has been very costly and ineffective. Their promotion only led to industrial concentrations and a further need for government regulation. The supposed export potential and economies of scale of the selected industry are not realized and only served to penalize downstream industries (also ultimately limiting the growth of the industry).

The lesson here is that restricting entry is not the best option. Restricting entry is not enough to realize economies of scale and the export potential of the industry. The profits earned may already be enough even by just serving the domestic market because the incumbent firms are able to charge high enough prices, being protected as they are from threats of new entry. Without the discipline of competition, there is no urgency to export and the firms are more likely to be content in just serving the domestic market.

Not only is restricting entry ineffective, it also creates additional costs and problems. The final outcome of restricting entry is an industrial concentration characterized by underutilized redundant capacity (one objective the restriction to entry is supposed to prevent). Hence, by the mid-1980s, the need for reforms has become urgently felt. Regulatory bodies such as the Iron and Steel Authority were abolished (and government assets sold). Nothing could be done with respect to the sunk costs of capital. The more pressing problem becomes that presented by concentration -- the possibility of abuse of dominant position. And this is not remedied by continued restriction to entry (which would only preserve its market power). Quite the opposite, the solution is to make the market contestable.

Indeed, in general, where the good is tradable, if concentration naturally results because of economies of scale, efforts should be made to make the market contestable. Then, the monopoly would not present a problem since it would not be able to earn excess profits because of the threat of entry. If there are sunk costs involved creating structural barriers to entry, the incumbent firm should be subject to the discipline of an anti-trust law to prevent anti-competitive actions.

Where the good is a natural monopoly

A problem arises, however, when the good is nontradable and the size of the market is too small for more than one producer to achieve economies of scale. The

same arguments above could hold. There could result a duplication of investment which could be a waste of resources if entry is not restricted. Nonetheless, wasteful as duplication of investments may be, the cost of duplication may still not be large enough to outweigh the cost of foregoing the competitive process.

The problem is when the production of the non-tradable good (or service) requires very large fixed capital. There may not even be increasing returns to scale but huge capital is required for production even for a minimum volume. In addition, it may also involve an essential facility, that is, a facility which is necessary input to another but is much too costly to be integrated into the production process. Then, duplication may indeed be socially and economically unviable and some regulation would be needed and justified. This is the case of the so-called natural monopolies.

The foremost examples of such cases are said to be in electricity (transmission) inter-island shipping, civil aviation and telecommunications. Towards this end, the government created corresponding regulatory bodies to address the problem. These are the Energy Regulatory Board (ERB) for electricity and the National Telecommunications Commission (NTC) for the telecommunications industry, The Philippine Ports Authority (PPA) and the Maritime Industry Authority (MARINA) for the shipping industry, and the Civil Aeronautics Board (CAB) for civil aviation industry. (These are discussed in more details in separate papers on telecommunications, power, shipping and civil aviation, in respective order by Serafica, Abrenica and the last two by Austria in this PASCN series of studies on competition.)

The two main regulatory measures these regulatory bodies employ include:

- The authority to issue, amend or revoke license/permit to operate in particular areas, and
- Control or fixing of rates/price.

For example MARINA has the right to determine what should be the capacity in all routes and on this basis, issue, amend and revoke franchise/permit to operate a route. It also regulates the passenger fares, freight rates and other related charges. In the case of telecommunications, although the franchise is granted by act of congress, NTC would need to grant a Provisional Authority (PA) for a carrier to be able to operate in a specific geographic area. It also sets and regulates the end-user price of the telecommunication service. There are other important measures the regulatory bodies use, depending on the nature of the industry that could impact on competition and efficiency. In the telecommunications industry for example, NTC formulates the policy on access to essential facility.

These regulatory measures are, at the outset, clearly anti-competitive and place limits on competition. However, the regulation, in each case, is intended to overcome market failure necessary for the development of the industry and should have pro-competitive effects. Efficiency is a stated objective. So is competition in the case of the NTC. Also, usually, the provision of a minimum level of good or service to unserved or underserved areas at an affordable price is an additional objective. This social objective is particularly important in the case of electricity, transportation and

telecommunications. This provides one of the main guidelines for regulating the rates - to allow for some cross-subsidization from more to less lucrative markets.

All these are worthy objectives. Nonetheless, considering the power that the regulator has, and the (monopoly) rights given the firm allowed entry, a careful review is necessary with respect to what is the real impact of the regulation. This requires a separate in-depth study of each industry. This paper can only point out the relevant issues that need to be looked into.

For a natural monopoly with huge fixed capital requirement, (e. g. the case of an essential facility), regulation could be justified. A lot still depends, however, on how the regulation is actually applied, and how necessary are the regulatory measures used. In this regard, there are a number of issues that need to be addressed.

First, there is a tendency for the regulation to cover a greater portion of the industry than necessary⁴ and for the regulator to "over-regulate." How much of the industry could be deregulated, and/or how much of the regulation can be relaxed? Are there elements/activities in the industry covered by the regulation which should be made subject to competition? If either of these possibilities is true, the cost of the regulation could be very high. Indeed, especially after the era of controls under the Marcos regime, there was increased realization of these costs of regulation which spurred the policy thrust towards deregulation in all these industries. Deregulation has mainly been done by easing entry into the industry and allowing more players to come in. The benefits of deregulation are still being felt-- in shipping, domestic air travel, and telecommunications in particular. Nonetheless, a lot more could probably still be done. Specifically, clearer delineation between segments (activities) in the industry which are natural monopolies and those which should be subject to more competition must be made.

Related to this is, how "essential" is the essential facility? Is there a clear policy access to essential facility? Is it essential enough to justify restricting entry of firms? For example, if the facility is not too difficult and costly to duplicate, then it is not an essential facility and entry should not be restricted. In other words, a stricter definition of essential facility is necessary. This would also help regulators identify and limit what segment of the industry could be considered a natural monopoly and is a necessary pre-requisite to a clear policy on access to the essential facility.

The third question is the policy of cross-subsidization. There is a need to re-evaluate the costs and benefits of cross-subsidization. This has been used as a reason for limiting entry (to prevent new entrants from "skimming off the top"). In the first place, it is very difficult to set the right prices and the cost of making a mistake could be high. In the second place, are there other alternatives to attaining the objective?⁵ These considerations make the assessment of how well objectives are satisfied very difficult to do.

Fourth, a problem common to all regulations is that the regulator could become subject to "capture." (Stigler 1968) The regulator could become beholden to

⁴ Due consideration should be given to the possibility of regulatory arbitrage.

⁵ An example is the assignment of credits to target beneficiaries.

the incumbent firm and would serve to protect the "competitor" rather than the competitive process. A review of the regulation should determine if and to what extent there is such regulatory capture. Perhaps, the task of regulation could in practice even be in the monopolist. What safeguards need to be put in place?

Fifth, another problem, also common to all regulations, is the tendency to use complicated and cumbersome procedures which could negate whatever pro-competitive effects there could be. Regular review to update and streamline the procedures would go a long way to increasing the efficiency of the regulatory process and the industry itself.

b. The case for financial sector regulation

The financial sector regulation can be justified on two grounds-- two cases of market failures: (1) the presence of asymmetric information, and (2) the presence of systemic risks. (Milo 2000) Perhaps the more compelling of the two is the second. The risk to one bank is a risk to all. The failure of one bank can cause the failure of others, if not the whole system. Thus regulation of the financial regulation is indeed well founded. However, there is regulation, and **there is regulation**.

Ideally, the regulation should address only the particular market failure. Hence, in the case of the financial sector, this means ensuring the stability and soundness of the banks and the payment system. This means prudential regulations. It does not mean limiting the number of firms per se. This means disallowing entry only if the entrant could not prove its soundness and stability.

However, as in the other cases discussed above, the problem of regulation is the tendency to "over-regulate." Are the regulations really just for the soundness and stability of the system? Or is entry unnecessarily restricted, weakening the discipline from competition?

Competition policies could only enhance the efficiency of the sector. This suggests that the competition policy objectives should generally apply to the financial sector. Thus, possibly another important issue is how to make the competition policy work for the financial sector. Of particular importance to the sector would be the competition policy rules on mergers and acquisitions.

The issues in competition policy for the financial sector are discussed in more details in Milo (2000).

c. Other industry-specific regulations

There are other industry-specific regulatory bodies. Possibly among the most important is the Land Transportation Franchising and Regulatory Board (LTFRB). Its primary objective is the provision of the service in all areas at affordable costs. There are also elements of public safety objectives. The same objective may also be important in other industry regulations. In most of the other cases, the objectives are for some social objectives that could be far removed from efficiency concerns.

In general, even if the stated objective were the overriding objective of the regulator, there is still the question of what would be the best way to do it. A different perspective from competition policy objectives may prove beneficial.

Table 2 provides a list of industry specific regulations.

Table 2
INDUSTRY-SPECIFIC POLICIES & REGULATIONS
WITH DIRECT IMPACT ON COMPETITION

| Industry | Regulatory Bodies/ Implementating Agencies | Functions/Objectives |
|----------------------------------|---|---|
| Banks and Financial Institutions | Bangko Sentral ng Pilipinas (BSP) | Supervision & regulation of the financial institutions---restriction on the grant of commercial bank licenses; Conduct monetary policy thru open market operations, imposition of reserve requirements & rediscounting transactions; Issue currency, lending to other banks & the government; manage foreign currency reserves; <i>Determination of the exchange rate policy</i> |
| Insurance companies | Insurance Commission (IC) | <i>Regulation</i> ---promulgate and implement rules & regulations governing insurance institutions, license insurance firms, brokers, agents and rehabilitate delinquent insurance companies; <i>Supervision</i> --- examine the financial condition of insurance entities, review their premium rates and evaluate their financial reports <i>Adjudication on the insurance industry</i> |

| | | |
|----------------------------------|--|--|
| Power generation & oil companies | Department of Energy (DOE) | <p>Develop and update the existing Philippine energy program which shall provide for an integrated and comprehensive exploration, development, utilization, distribution, and conservation of energy resources, with preferential bias for environment-friendly indigenous, and low-cost sources of energy;</p> <p>Establish and administer programs for the exploration, transportation, marketing, distribution, utilization, conservation, stockpiling, and storage of energy resources of all forms, whether conventional or non-conventional;</p> <p>Regulate private sector activities relative to energy projects as provided for under existing laws;</p> |
| | National Power Corporation (NAPOCOR) | <p>Responsible for the strategic and rational development of the Philippine power grids and the construction of generating facilities, in cooperation with the private sector</p> |
| | Energy Regulatory Board (ERB) | <p>Assure adequate & continuous supply of crude oil, electric power and other energy sources at reasonable & stable prices;</p> <p>Protect the oil industry, electric utilities & other entities & persons engaged in the importation, exportation, marketing & distribution of energy sources & products, & ensure that these entities and persons operate under the conditions of orderly & economic competition</p> <p>Responsible for fixing & regulating the rate of schedule of prices of piped gas to be charge by duly franchised gas companies (implementation of full deregulation)</p> |
| Telecommunications Companies | National Telecommunications Commission (NTC) | <p>Independent regulatory body that exercises jurisdiction over the supervision, adjudication and control over all telecommunications services;</p> <p>Responsible for issuance of licenses to operate telecommunications systems, facilities & monitoring of compliance to rules & regulations</p> |
| Land Vehicles | Land Transportation Franchising and Regulatory Board | <p>Prescribes and regulates routes of service, economically viable capacities and zones or areas of operation;</p> |

| | | |
|------------------------------------|---|--|
| | (LTFRB) | <i>Issue, amend, revise and suspend or cancel certification of Public Convenience or permits; Determine, prescribe, and approve reasonable fares & rates for public land transportation services; among others</i> |
| Shipping industry | Maritime Industry Authority (MARINA) | <i>Regulates and supervises both domestic & overseas shipping industries; Evaluates & processes applications to increase/change passenger fares, freight rates and other charges related to the operation of domestic public water transportation services</i> |
| Air commerce companies | Civil Aeronautics Board (CAB) | <i>Responsible for the establishment and enforcement of standard airline/airfreight rates, fees & other charges based on studies of airline traffic & volume of passengers and cargo; Maintains an accounting system for all air carriers & conducts audits to determine whether air carriers have complied with bilateral agreements & local policies</i> |
| Port operators & arrastre services | Philippine Ports Authority (PPA) | <i>Establish, develop, regulate manage and operate a rational national port system in support of trade and national development Regulate port services, selection of port operators and collection of fees for port-related services</i> |
| Toll | Toll Regulatory Board | <i>Authority to approve initial toll rates, review & approve toll rates</i> |
| Water | Local Water Utilities Administration (LWUA) | <i>Undertake water supply development outside Metro Manila thru the creation of Water Districts; Establish minimum standards & regulations (e.g. construction materials & supplies, maintenance & operation) for local water utilities as well as monitor & evaluate local water standards</i> |

| | | |
|---------|----------------------------------|--|
| Housing | National Housing Authority (NHA) | <p><i>Provide affordable and adequate housing for homeless low-income families & afford them access to social services and economic development</i></p> <p><i>Harness and promote private participation in housing ventures in terms of capital expenditures, land, expertise, financing & facilities for the sustained growth of the housing industry</i></p> |
|---------|----------------------------------|--|

4.2 Direct government equity participation

As implied in the discussion above, one reason for direct equity participation could be the promotion of an industry. Such strategy was most widely used during the Marcos administration. The social profitability is considered to be high but due to some distortions (e. g. high private risks), the private sector is not interested to enter the market because it is not privately profitable. (Of course, the government could simply just provide fiscal and other incentives to make the activity privately profitable.) Perhaps a more justifiable objective for the government equity participation is the production or provision of a public good. Possibly another reason is to provide stability in the market.

Table 3 provides a list of these existing public enterprises.

Whatever the objective for the government equity participation, what is more important to consider is how it impacts on competition. The public enterprise may be enjoying undeserved, unnecessary and unfair advantages, e. g., in terms of tax privileges, access to credit and loan guarantees. This could drive the more efficient private firms out of the market.

Privatization has been part of the major reforms being implemented since the Aquino administration. For some years, asset privatization has been a source of badly needed revenues. However, although it has been an important source of revenue especially during the initial years, privatization is now viewed more as a tool to encourage competition. This is part of the effort of reforming public enterprises.

Table 3
LIST OF SOME GOVERNMENT CORPORATIONS

| Department | Classification | Name | Activity/Purpose/Objectives |
|------------|-----------------------|-----------------------------|---|
| DA | Non-Financial GOCC | National Dairy Authority | <i>Milk & dairy products production</i> |

| | | | |
|--------|--------------------|--|--|
| | Major Corp. | National Irrigation Administration | <i>Provides nationwide irrigation facilities</i> |
| | Non-Financial GOCC | National Tobacco Administration | <i>Tobacco production & development</i> |
| | Non-Financial GOCC | Philippine Cotton Authority | <i>Production and development of cotton industry</i> |
| | Non-Financial GOCC | Philippine Rice Research Institute | <i>Conduct and coordinates rice research and development</i> |
| DOE | Major Corp. | National Electrification Administration | <i>Predominant lender of electric cooperatives which distributes power largely in rural areas</i> |
| | Major Corp. | Philippine National Oil Company | <i>Oil refining, exploration & development of non-oil products</i> |
| DOF | GFI | Philippine Deposit Insurance Corporation | <i>Insured bank deposits of depositors</i> |
| DOT | Non-Financial GOCC | Philippine Convention & Visitors Corporation | <i>Develop and adopt an Integrated Tourism Marketing Plan to create an ideal destination image and providing a wholesome experience for foreign and local visitors;</i> |
| DTI | Major Corp. | National Development Company | <i>Establish enterprises to fill up critical gaps in the input-output structure of Philippine commerce & industry when the private sector is unwilling to engage due to risk undertaking</i> |
| | Non-Financial GOCC | Philippine International Trading Corp. | <i>Engage in both export & import trading on new or non-traditional products or markets not normally pursued by private sector</i> |
| DOTC | Major Corp. | Light Rail Transit Authority | <i>Transportation</i> |
| | Major Corp. | Philippine National Railways | <i>Transportation</i> |
| | Non-Financial GOCC | Philippine Postal Corporation | <i>Mailing system and postal services</i> |
| Others | GFI | Home Insurance & Guaranty Corporation | <i>Provides housing insurance and guarantee</i> |

| | | | |
|--|--------------------|--|---|
| | GFI | National Home Mortgage Finance Corporation | <i>Provide long-term buyer's financing assistance for housing; specialized on community mortgage</i> |
| | Non-Financial GOCC | Philippine Amusement & Gaming Corporation | <i>Establish and operate clubs and casinos for amusement and recreation, including sports gaming pools and such other forms of amusement & recreation</i> |

Sources: Administrative Code of 1987, E.O 292; Homepage/Websites of various government agencies

Various research studies have shown publicly owned and run corporations to be less efficient than private enterprises. This is due to a number of factors. First is the hiring and firing scheme which is constrained by the civil service regulations that make it extremely difficult to fire and hire employees. The second factor is the incentive and compensation structure. Third is lack of accountability. These factors, among others, deprive the public enterprise of the usual motivation for profit maximization as is present for private firms.

However, transfer of ownership alone would not ensure (may only transfer rents) increased efficiency if the necessary conditions for a competitive market is not set forth beforehand. Indeed, the problem may not be whether to transfer ownership or not but rather how the competition process and discipline could be introduced. If there would be transfer of ownership, all unnecessary advantages previously enjoyed by the firm should be removed and competitive neutrality should be ensured. These issues need to be examined further in the reforms of public enterprises.

4.3 Other regulatory restrictions

The other regulatory restrictions could range from explicit restraints to entry requiring firms to obtain permit or license to operate in a particular market to stringent procedural and other requirements making entry to a market difficult. These include among others:

- a. Local Government Code provisions on licensing and zoning,
- b. Lengthy and cumbersome bankruptcy and insolvency laws forming exit barriers,
- c. Labor Code provisions which restrict flexibility of firms to downsize or shut down also forming exit barriers,
- d. Intellectual property rights protection,
- e. Government procurement policy, and
- f. Business registration requirements.

The rationale for the restriction would vary from public safety to monitoring and other reasons. Table 4 provides a listing of some special laws and provisions creating regulatory restrictions.

In the first, the local government is given leeway in its efforts to pursue its own strategy for development. While some autonomy should be exercised by the Local Government, they should be made aware if their actions could have serious detrimental impact on competition and efficiency, even if in the end they have the final decision.

In the second, these exit provisions could form entry barriers as well.

The government policy on intellectual property rights (IPR) is intended to encourage innovation, a necessary condition for dynamic efficiency. Though it could grant temporary monopoly rights to the holder of the IPR, this should be balanced against this future dynamic gains from innovation.

Table 4
SPECIAL LAWS & AGENCIES AFFECTING COMPETITION

| Laws | Provision/Purpose | Implementing Agencies | Functions |
|--|--|---|---|
| Local Government Code (RA 7160, 1991) | Licensing & Zoning or Land Classification Taxation | Local Government Units (LGUs) | Grant franchises & permits or licenses within the locality Grant of tax exemptions, incentives or reliefs to entities engaged in “community growth-inducing industries” |
| Insolvency law (Act No.1956) Bankruptcy Law | Seeks to effect an equitable distribution of the insolvent’s property among creditors; Deals with suspension of payments, the relief of insolvent debtors, the protection of creditors and the punishment of fraudulent debtors | <i>Private Corporations</i> ----- Securities & Exchange Commission (SEC) <i>Banks & Financial Institutions</i> ----- Bangko Sentral ng Pilipinas (BSP) | Conducts hearings in the case of dissolution affects the rights of any creditor having claim against the corporation; Appoint a receiver to take charge of the liquidation of the corporation Appoint a conservator to take charge of the assets & liabilities of the bank or non-bank as well as assume management (if in a state of continuing inability to maintain a condition of solvency & liquidity) |

| | | | |
|---|--|--|---|
| | | | <p><i>Designates a receiver to take charge of assets & liabilities and administer to the benefit of creditors (if continuance in business would involve probable loss to depositors & creditors)</i></p> <p><i>Assign liquidator to take over the functions and shall convert the banks assets to money for the purpose of paying off its creditors (if insolvent & cannot resume business)</i></p> |
| <p>Corporation Code (BP 68, 1980)</p> <p>Revised Securities Act (BP 178, 1982)</p> | <p>Rules regarding mergers & consolidations and the acquisition of all or substantially all the assets or shares of stocks of corporations</p> <p>Prohibits & penalizes the manipulation of security prices & insider trading</p> | <p>Securities & Exchange Commission (SEC)</p> | <p><i>Absolute jurisdiction, supervision and control over all corporations, partnerships and associations in the Philippines; as a regulatory agency it has the exclusive jurisdiction to hear and decide on cases involving fraud and misrepresentation committed by corporate officers and their organizations;</i></p> <p><i>Empowered to look into intra-corporate problems of corporations, issue injunctive relief, subpoena and subpoena duces tecum; impose fines and penalties; and even suspend or revoke the certificate of registration of any erring establishment after a proper hearing.</i></p> |
| <p>Labor Code (PD 442)</p> | <p>Provide adequate protection to labor by stipulating the minimum conditions of labor, labor relations, formation of workers organizations & unions, termination & retirement benefits of workers</p> | <p>Bureau of Labor Relations</p> <p>National Labor Relations Commission</p> | <p><i>Provide orientation to workers on their rights & privileges under existing laws & regulations;</i></p> <p><i>Develop schemes and projects for the improvement of the standards of living of workers & their families</i></p> |

| | | | |
|--|--|---|---|
| Intellectual Property Code (RA 8293, 1997) | Protection of patents, trademarks and copyrights and the corresponding penalties for infringement | Intellectual Property Office (IPO) | <i>Examine applications for grant of letters, patent for inventions and register utility models and industrial designs; register technology transfer arrangements & settle disputes; Promote the use of patent information as a tool for technology development Administratively adjudicate contested proceedings affecting intellectual property rights</i> |
| Budget Reform PD 1177 RA 5183 | Protecting locally-manufactured or produced articles over foreign made products Purchase of locally manufactured products Reserving to Filipinos & Filipino-owned corporations the exclusive right to enter into contracts with any GOCC's, company, agency or municipal corporation for the supply of materials, goods, & commodities | State Accounting & Auditing Development Office, Commission of Audit (COA) | <i>Develop & implement a comprehensive audit program that shall encompass an examination of financial transactions, accounts, & reports, including evaluation of compliance with applicable laws & regulations; Institute control measures through the promulgation of auditing rules & regulations governing receipts, disbursements and uses of funds & property consistent with the total economic development efforts of the government</i> |

Sources: Abad, Anthony. 1999. "Recommendations for Philippine Anti-Trust Policy and Regulation

USAID. 1992 "Barriers to Entry Study" .Volume I.
Administrative Code of 1987, E.O 292

Government procurement policies are among the issues being examined in the international fora on trade. There is increasing concern about how these could violate the spirit of fair trade espoused by the WTO. Not only is there this international dimension of the impact of government procurement policies, there should also be more immediate and local concern about its impact on domestic competition.

Finally the cumbersome process of registration procedures itself could be an important source of barriers to entry. This is especially true for small and medium scale industry. The checklists of requirements doing business in the Philippines and

business registration in Tables 5 and 6 illustrate the long process and numerous requirements a prospective business needs to hurdle just to be registered. This could more especially prove difficult for small and medium enterprises. Regular review of these procedures should be done to simplify and modernize the process.

To summarize, these regulations are supposed to serve some objectives, even pro-competitive objectives. Nonetheless, there is a clear need to re-evaluate these policies and review whether such policies and regulations could pass a "competition" test or, if not, if they could be justified on grounds of public welfare in general or the objectives they are supposed to achieve in particular.

5. Other Government Policies and their Interface with Competition Policy Objectives

The second group would include government policies aimed at achieving various other objectives that are not overtly related to competition but would nonetheless have significant, though less direct impact on the state of competition. The list in this second group could be long but the major policies would include among others the following:

- Industrial policies: investment policy, export promotion, foreign investment, and regional development policies,
- Agricultural policies, and
- Environmental policy and regulations.

(Please refer to Table 7)

The last could have direct impact on barriers to entry as well but is included here because of other social objective that is paramount to it. Also, there is no doubt there are other major policies not included which would have a significant interface with competition policy objectives. This, however, hopefully illustrates the importance of examining this interface and lessons that could be obtained from it for the others.

These policies are supposedly intended to serve other explicit objectives-- the basically development of the sector, ultimately benefiting the economy as a whole. The question is how much should competition policy also be considered.

Table 5

DOING BUSINESS IN THE PHILIPPINES

(Checklist)

This checklist is a general guide which investors may find helpful in preparing to do business in the Philippines.

An investor needs only to undertake the applicable combination of activities. Some can be done simultaneously it is advisable to seek the assistance and briefing of the Board of Investments One-Stop Action Center (BOI-OSAC), the Bureau of Trade Regulation and Consumer Protection (BTRCP), the Philippine Economic Zone Authority (PEZA), and the Securities and Exchange Commission (SEC).

Getting Started

General Registration Requirements

Investors setting up business in the country will have to comply with the following general requirements:

- Registration of corporations and partnerships---Securities and Exchange Commission (SEC)
- Registration of business name/single proprietorship---Bureau of Trade Regulations and Consumer Protection (BTRCP)
- Registration for incentives availment under Executive Order 226---Board of Investments (BOI)
- Registration of export firms (for those locating in any of the country's export processing zones and availing of incentives)---Philippine Economic Zone Authority (PEZA)
- Registration of foreign investments for purposes of capital repatriation and profit remittances---Banko Sentral ng Pilipinas (BSP)
- Securing Tax Identification Number (TIN) ---Bureau of Internal Revenue (BIR)
- Securing locational clearance/business permit for firms locating in Metro Manila---Metro Manila Authority (MMA)
- Securing building permit and license to do business---City Halls/Municipal Offices in the localities where the business will be set up
- Securing an employer's SSS number Social Security System (SSS)
- Securing membership in the government health care benefits system Medicare
- Securing electric services connection ---Manila Electric Co. (MERALCO) for business in MERALCO franchise area; local electric utility firms for companies locating in non-MERALCO franchise area
- Securing Water services---Metropolitan Waterworks and Sewerage System (MWSS) for firms locating in Metro Manila and Local Water Utilities Administration (LWUA) for firms locating outside Metro Manila

OPERATIONAL REQUIREMENTS

Certain requirements will have to be complied with by the enterprise while in operation, expansion and/or diversification.

A. While in operation the following need to be accomplished:

- Reportorial requirements; amendment of articles of incorporation
Securities and Exchange Commission (SEC)
- Reportorial requirements; registration of business/expansion for incentives
Board of Investments (BOI)
- Regular tax payments
Bureau of Internal Revenue (BIR)
- Registration of Customs Bonded Warehouse
Bureau of Customs (BOC)
- Opening of Letter of Credits (L/Cs)
Authorized Agent Banks (ABBs)
- Certificate to import duty-free
Board of Investments (BOI)
- Authority to load/certificate of origin
Bureau of Customs - Export Coordinating Division (BCECD)
- Information sheet for first-time exporters
Banko Sentral ng Pilipinas (BSP)
- Payment of wharfage fees/exemption from payment
Philippine Ports Authority (PPA)

B. Special Permits/Clearance/Registration

Special permits/clearances/registration are required when pursuing the following projects/activities:

- Expatriates' visas
Bureau of Immigration (BI)
- Alien Employment Permit (AEP)
Department of Labor and Employment (DOLE)
- Clearance for garment exporters/quota allocation
Garments and Textile Export Board (GTEB)
- Registration for operation of Customs Bonded
Manufacturing Warehouse (CBMW)
Bureau of Customs (BOC)
- Environmental compliance certification
Environmental Management Bureau, Department of Environmental and Natural Resources (DENR)
- Projects involving land use/conversion
Housing and Land Use Regulatory Board (HLURB), National Housing Authority (NHA), Department
of Agrarian Reform (DAR)

- Permit to construct/operate pollution-control devices
Department of Environmental and Natural Resources (DENR)
- Trademarks/patents registration
Bureau of Patents, Trademarks, and Technology Transfer (BPTTT)
- Registration of power-generation projects
National Power Corporation (NAPOCOR)
- Philippine Standard (PS) Quality Mark to ensure that locally-manufactured consumer products conform to Philippine standards
Bureau of Products Standards (BPS)
- Import Commodity Clearance (ICC) Quality Mark to ensure that imported consumer products conform to Philippine standards
Bureau of Product Standard (BPS)
- Clearance for projects which involve food, chemicals, and others
Bureau of Food and Drug (BFD)
- Registration of tourism projects
Department of Tourism (DOT)
- Franchise for mass transit operation
Land Transportation, Franchising and Regulatory Board (LTRFB)
- Telecommunication projects
National Telecommunications Commission (NTC)
- License/clearance for defense-related projects
Department of National Defense (DND)/ Philippine National Police (PNP)
- Registration of advanced technology
Department of Science and Technology (DOST)
- Clearance for health-related projects
Department of Health (DOH)
- Clearance for oil exploration activities
Office of Energy Affairs (OEA)
- Acquiring mining rights
Bureau of Mines and Geo-Sciences (BMG)

C. Special Permits/Clearances for selected export businesses

Export of products will need clearances and permits prior to every shipment:

- Clearance for export of animal and animal by-products
Bureau of Animal Industry (BAI)
- Clearance for plant export
Bureau of Plant Industry (BPI)
- Clearance for export of food, drugs, and chemicals
Bureau of Food and Drug (BFD)
- Clearance/quota for coffee exports
International Coffee Organization Certifying Agency (ICOCA)
- Clearance for quota allocation of garment exports
Garments and Textile Export Board (GTEB)
- Clearance for export of fisheries and other aquatic products
Bureau of Fisheries and Aquatic Resources (BFAR)
- Special documentation certificate for preferential treatment of handicrafts export
Department of Trade & Industry-National Capital Region (DTI-NCR)
- Export clearance for coconut products
Philippine Coconut Authority (PCA)
- Commodity clearance for natural fibers export
Fiber Industry Development Authority (FIDA)

AVAILABLE FRONTLINES

A. One-Stop Action Centers (OSAC)

Designated One-Stop Action Centers provide facilities and services which enable the investor to obtain necessary investment information and documentation in one physical location. These OSAC are:

- One-Stop Action Center for Investments - at the Board of Investments (BOI)
- One-Stop Export Documentation Center - at the International Trade Center Complex
- One-Stop Import Processing Center - at the Bureau of Import Services (BIS)
- One-Stop Shop Tax Credit Center - at the Department of Finance (DOF)
- One-Stop Action Garments Export Assistance Center - at the Garments and Textile Export Board

B. Technical Services and Quality Control

Agencies listed below provide various quality control and technical services to investors:

- Cottage Industry Technology Center (CITC)
- Philippine Shippers Council (PSC)
- Philippine Textile Research Institute (PTRI)
- Product Development and Design Center of the Philippines (PDDCP)
- National Manpower and Youth Council (NMYC), Department of Labor and Employment (DOLE)

C. Export Marketing

When in need of export marketing support, the investor can consult various government agencies for free assistance in:

- Matchmaking between exports and buyers/raw material suppliers
Export Assistance Network (Exponet)
- Market information, strategy, product research, and foreign trade assistance
Bureau of Export Trade Promotion (BETP)
- Garments export assistance
Garments and Textile Export Board - One Stop Action Center (GTEB-OSAC)
- Trading with Socialist countries
Philippine International Trading Corporation (PITC)
- Trade fairs/exhibitions
Center for International Trade Exposition and Missions (CITEM)
- Product development and improvement
Product Development and Design Center of the Philippines (PDDCP)
- Subcontracting facilities between contractors and subcontractors
National Subcontractors Exchange (Subconex)

Aside from these frontline assistance centers, the investors may also approach different industry association and business chambers.

Table 6

**REQUIREMENTS AND SUPPORTING DOCUMENTS
FOR BUSINESS NAME REGISTRATION**

1. Fill out completely the application form and submit to the Department of Trade & Industry Provincial Office where the business is located.
2. If Single Proprietorship.
 - a. The applicant must be a Filipino Citizen, of majority age (18 years or over) and must attached two (2) passport size pictures taken not more than one (1) year preceding this filing.
 - b. Natural-born Filipinos whose names are suggestive of an alien nationality (example: Chua, Tan, Taylor, etc.) attach proof of citizenship, e.g., PRC ID, birth certificate or voter's ID.
 - c. For Citizen of the Philippines by:
NATURALIZATION - submit photocopy of naturalization certificate and oath of allegiance or identification card issued by the Commission on Immigration & Deportation and present original copies for comparison.
ELECTION - submit photocopy of affidavit of election or identification card issued by the Commission on Immigration and Deportation and present original copies for comparison.
3. If Partnership / Corporation / Cooperatives / Other Judicial Entities,
 - a. Submit photocopy of SEC certificates of registration, articles of incorporation / partnership and by-laws duly signed by authorized representative/ partner.
 - b. Cooperative must be registered first with Cooperatives Development Authority (CDA) and submit copy of certificate thereof.
4. If Franchise Holders of Business Name - submit latest franchise agreement.
5. If Foreign Investor, he must submit the following:
 - a. Alien certificate of registration.
 - b. Accomplished DTI Form No. 17 under R.A. 7042
 - c. Written Appointment of Filipino Resident Agent
 - d. Authority to verify bank accounts/bank certificate of deposit
 - e. Proof of inward remittance of foreign currency for non-resident alien and Bank Certificate of Deposit for resident alien.
 - f. Copy of valuation report from Central Bank if investment includes assets other than foreign exchange.
 - g. Certification from resident alien not seeking remittance of profit or dividends.
 - h. Clearance from other involved agencies such as Department of Science and Technology, Philippine National Police, Etc.
 - i. In case of alien retailer, latest permit to engage in retail business per R.A. 1180
 - j. If corporation/partnership SEC certificate of registration and Certificate of Authority from SEC.
6. If the business name, together with business establishment was acquired thru sale, transfer or assignment, applicant must comply with the Bulk Sales Law, by submitting the following:
 - a. Affidavit of vendor stating that at the time of sales, he had no creditors or if there were creditor/s, copy of notice to them.
 - b. Deed of sales, assignment or transfer
 - c. Inventory of properties sold, assigned or transferred
 - d. Payment of fee as prescribed by the government
 - e. Original certificate of business name registration of vendor for cancellation.

Additional requirements may be imposed on case-to-case basis on actual examination and processing of the application.

Table 7
MAJOR POLICIES WITH COMPETITION POLICY INTERFACE

| Policy Areas | Regulatory Bodies/ Implementating Agencies | Purpose/Functions/Objectives |
|---|---|---|
| Industry & Investments Policy | Department of Trade and Industry (DTI) | <i>Formulate and implement policies, plans and programs relative to the development, expansion, promotion and regulation of trade, industry and investments</i> |
| <ul style="list-style-type: none"> ✓ Export Promotion ✓ Promotion of Catalytic Industry ✓ Regional Development | Board on Investments (BOI) | <p><i>Coordinate the formulation and implementation of short, medium and long term industrial plans as well as promoting investments in the country in accordance with national policies and priorities;</i></p> <p><i>Register, monitor and grant investment incentives to individual enterprises;</i></p> <p><i>Formulate policies and guidelines aimed at creating an environment conducive to the expansion of existing investments</i></p> |
| <ul style="list-style-type: none"> ✓ Foreign Investment Policy | Philippine Economic Zone Authority (PEZA) | <i>Tasked with the establishment, operation and management of world-class economic zones or ecozones throughout the country</i> |

| | | |
|--------------------|---|---|
| | Garments and Textile Export Board (GTEB) | <p><i>Formulation of negotiation strategies and the actual negotiation of bilateral trade agreements with major importing countries such as the United States, European Union, Canada, and Norway;</i></p> <p><i>Overall administration and allocation of export quota, processing and issuance of garment and textile export clearances, bonded manufacturing warehouse licenses, and authority to import raw materials;</i></p> <p><i>Conduct of promotional and developmental activities that aim to diversify and expand export markets and optimize quota utilization.</i></p> |
| | Bases Conversion and Development Authority (BCDA) | Administers and develops former military bases into other productive uses |
| | Subic Bay Metropolitan Authority (SBMA) | <p>Administer and develop the Subic Bay Freeport (SBF) into a self-sustaining industrial, commercial, financial and investment center to generate, among others, employment opportunities in and around the Zone;</p> <p><i>Establish and regulate the operation and maintenance of utilities, services and infrastructure;</i></p> <p><i>Operate directly and indirectly tourism-related activities; and protect the Freeport's forests.</i></p> |
| | Clark Development Corporation (CDC) | <i>Manage and develop the Clark Special Economic Zone into a premier economic center and model township promoting industrial, service, commercial, recreational, residential and ecological development.</i> |
| Agriculture Policy | Department of Agriculture (DA) | <i>Responsible for planning, formulation, execution, regulation and monitoring of programs & activities relating to agriculture, food production & supply;</i> |

| | | |
|--|--|---|
| | National Food Authority (NFA) | Responsible for food security and stabilization of supply and prices of rice, Corn, wheat & other grains & food stuffs; implement subsidized marketing strategy |
| | Sugar Regulatory Administration (SRA) | Responsible for the regulation & development of the Sugar industry including the allocation of sugar production & export quota |
| | Philippine Coconut Authority (PCA) | Responsible for the regulation & development of the Coconut industry |
| Environment Policy ✓ Establishment of Environment Impact Assessment System (EIA) ✓ Establishment of ambient, effluent & input standards ✓ Comprehensive Air Pollution Control Policy; ODS Phaseout | Department of Environment & Natural Resources (DENR) | Administrative agency compelling compliance on environmental laws & responsible for issuance of environmental compliance certificate (ECC) & environmental permits— Authority to Construct (AC) and Permit to Operate (PO) |
| | Pollution Adjudication Board | Empowered to order the cessation of environmentally harmful activities through Cease-and-Desist-Orders |
| | Environment Management Bureau | Recommend possible legislation, policies & programs for environmental management & pollution control; formulate environmental quality standards for water, air, land, noise & radiations; formulate rules & regulations for proper disposition of solid waste, toxic & hazardous substances; recommend rules & regulations for environmental impact assessments & provide technical assistance for their implementation & monitoring |

Sources: Administrative Code of 1987, E.O 292
 Medalla, Erlinda.1997. "Philippine Industrial Policy and the Environment: Integrative Report"
 Homepages/Websites of Various Government Agencies

5.1 Industrial Policies

Turning to the first policy, a major tool for industrial development is the investment policy. This is largely embodied in the Omnibus Investment Code (OIC). The OIC is mainly administered by the Board of Investments basically through the promotion of selected activities in its Investment Priorities Plan (IPP) and the granting of fiscal incentives. The OIC also has other provisions aimed at other specific objectives, of which the more important ones include: (a) regional development objectives specifically through the promotion of industrial estates, and (b) promotion of Foreign Direct Investment (FDI).

For the investment policy as a whole, the objective is to aid in industrial growth and development. The thinking behind this is that there are market failures which prevent the industrial sector from developing naturally. Indeed, there is greater conscious consideration of this rationale for role of investment policy. This is reflected in the shortening of the list of industries in the Investment Priorities Plan (IPP), and moving towards a more promotional body. The "measured capacity" concept in the Omnibus Investment Code which limits granting of incentives when a certain capacity (some optimum scale) is reached, clearly anti-competition in nature, is not followed in practice. There is a move towards the "greening" of incentives, realizing externalities involved. Export promotion remains in the list of priority. As noted above, regional dispersal of industries and promotion of regional investment have been among the stated goals of the Philippine government.

These are arguably desirable objectives. Nonetheless, the industrial strategy chosen has probably been too preoccupied with simply trying to overcome the failures of the market (real or merely perceived). An obvious strategy which has been overlooked is to proactively support competition policy for industry, since their objectives in a large part actually merge. Their objective of industrial development policy is to enhance efficiency coincide with competition policy objective. Indeed, could competition policy actually serve as one of policy tool for industrial development (together with trade, fiscal and monetary policies)? Was it even deliberately considered? Or, on the contrary, are there anti-competition effects which unintentionally go against the competition policy objective (serving to defeat their purpose)? One that comes to mind is the inherent bias of an incentive granting system against the entry of small and medium scale industries.

Of particular importance is the policy on foreign direct investment. Restrictions on foreign equity have a direct impact on entry of firms. Specifically, they represent (policy-induced) structural barriers to entry. Substantial liberalization was effected by the 1991 Foreign Investment Act which changed the regime from a highly regulatory system of positive list where foreign equity is fully or partially allowed, to a more liberal system of negative lists where only those in the list are not allowed 100 percent foreign equity participation. Recently, some liberalization was implemented in retail trade with the passing of the Retail Trade Act. This could prove

to have a big impact on competition. It would also compliment well the effects of trade reforms.

Foreign equity participation is still limited for many sectors and this is supposedly for some other social objectives (national security, sovereignty, and others). Clearly, there is a need to re-examine the issues to evaluate whether the restriction in fact serves the stated objectives, and assess the benefits and costs of limiting competition with such restrictions.

5.2 Agricultural Policies

With respect to agricultural policy, a basic rule should also be for government to intervene only when market fails. However, for agricultural policies, there appears to be the additional, equally important (possibly more so in some cases), equity objective. This is where it could run counter to competition policy objectives. Nonetheless, if such trade offs exist, are they justified? That is, would benefits (from equity considerations for example) outweigh costs (e. g. efficiency losses from foregoing competition objectives).

In particular, agricultural policy still relies on tariff policy tools and other trade controls (anti-competition). This is supposedly to protect income of farmers (equity objective). Are the costs of protection commensurate to the benefits of increased income for the farmer? Is protection even reaching the farmer. These are important questions to ask.

Also very important to examine are the other policies which have anti-competition elements. These are the regulations implemented by the National Food Authority (NFA) and Sugar Regulatory Administration (SRA). Studies of the impact of these anti-competition policies on efficiency and consumer welfare should be done.

5.3 Environmental Policy and Regulations

Perhaps the policy with most direct interface with competition policy among the list is environmental policy and regulations. The environment is a public good characterized by externalities. To illustrate, our air and water system would have a limited absorptive capacity, beyond which environmental costs become acute. Thus environmental standards need to be set and some regulations should be put in place to efficiently manage the environment and promote sustainable development. When feasible, market-based instruments should be used which would allow the market to perform its function. However, the use of command and control measures may, in some cases, be unavoidable (whether due to administrative constraints or other reasons) and more intrusive environmental regulations may be necessary.

Environmental regulations for example, include pre-entry conditions as the environmental impact analysis (EIA), the environmental clearance certificate (ECC) and some other permits or licenses. These clearly create barriers to entry. Hence, there is evident conflict between environmental and competition policy objectives.

Should environmental concerns be the overriding objective? The ideal answer is that both should be considered-- environmental benefits must be weighed against costs from loss in competition. This weighing of costs and benefits, however, need not be done directly. What is necessary is to implement measures that would lead to internalization of external costs. If environmental costs were internalized properly, then overall welfare is optimized. That is so long as good environmental policy is in place and adequately enforced, whatever economic policy adopted would not impose undue burden, because there would be "correct" pricing of scarce environmental resources. Indeed, to optimize welfare there should both be good environmental policy and good economic policy (including competition policy).

Pricing economic resources below costs would lead to waste of resources. Pricing above costs, on the other hand, would impose undue burden on industry, unnecessarily raise costs and ultimately reduce overall welfare. The former comes from inadequate environmental policy and/or lax enforcement of it. The latter arises from too stringent policy and administration.

Environmental policy and regulations, however sound they may be, would be ineffective if not complemented by transparent and efficient implementing agency. The problem is, difficult as it may be to formulate sound environmental policies, it is sometimes even more difficult to administer and implement them properly. Nonetheless, the government must ever be reviewing the relevance and soundness of environmental policies, as well as the effectiveness of its administration, keeping in mind in both cases the possible impact on the competitive environment.

In sum, what all these imply is a need to closely re-examine government policies in the light of competition objectives. Such an exercise would surely bring new perspectives which would make for a more efficient administration of policy and identification and implementation of needed reforms.

6. Summary and Conclusions

Almost anything the government does could have an impact on competition and competition policy objectives. Although, competition is not the goal in itself, its role in improving efficiency and allocating efficient resources make it a key element in the government's pursuit of economic and social objectives. And if some government policy runs contrary to competition principles and guidelines, there is enough basis to at least re-examine this policy. Evaluating policies in the light of competition policy objectives does not imply prioritizing competition and efficiency objectives over others. It would only make more transparent the trade-offs and the decision making process.

The paper examined three sets of government policies in terms of how they relate to the objectives of competition. The first is trade policy. The second group includes government regulations and restrictions directly affecting competition. The third group includes other major government policies with other development objectives but has interface with competition policy objectives. The objective is to clarify what important trade-offs may exist and how and possibly when conflicts between government policies and competition policy objectives arise.

In general, the paper points out the need to bring in more closely the principles of competition policy into analyzing and evaluating government policies. This is especially true in the pursuance of needed reforms in government regulations. Recognizing its role in the major government policies will shed more light into how effective these policies are. Indeed, competition policy would provide a new and different perspective which could help formulate a more effective and dynamic development policy for the Philippines.

Finally, it could, of course, very well be the case that the government policy in question, however much in conflict it might be with competition policy, could arguably be the appropriate development strategy. The review of such policy in light of competition policy objectives should not be intended to summarily dismiss such strategy, even if it limits the competitive process, if it would indeed lead to greater efficiency and increased welfare. The review would, in the end, even build a stronger case for it.⁶

⁶In practice, however, considering the limited resources available to the government, such policies or strategy with more apparent benefits to society, should be low in the priority for review. Indeed, there may be a need to focus very selectively on certain key policies.

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