

CCCS-ESS Essay Competition 2022 School Category First Prize

Environmental Sustainability: The role of competition and consumer protection laws and policies

Abstract

This essay explores the role of competition and consumer protection laws in promoting environmental sustainability in light of the deteriorating quality of the environment.

Section 1 establishes the context of environmental sustainability and the role of firms, highlighting the growing role of firms in promoting environmental sustainability. As key elements of private initiatives, competition and consumer protection laws play an essential role in driving environmental sustainability.

Section 2 analyses the various causes of market failure in the market for sustainable initiatives. This includes demand-side market failure due to information asymmetry and positive externalities, along with supply-side market failure due to first-mover disadvantage. This section also illustrates the impacts and introduces an outline of possible ways to reduce market failure such as collaboration among firms, and further details the environmental benefits of collaboration.

Section 3 examines the role of competition law in driving environmental sustainability. Competition law can promote sustainability by enhancing productive and dynamic efficiency, but it also has the potential to impede sustainable collaborations by firms. This is exacerbated by the legal uncertainty surrounding sustainable collaborations given the lack of explicit guidelines and precedent cases. I argue that environmental benefits should be considered as economic efficiencies when assessing the anticompetitive effects of sustainability agreements given the positive externalities generated, and this would be consistent with Singapore's approach to

competition law. These benefits can be measured with established methods of pricing environmental benefits such as shadow pricing.

Section 4 addresses how consumer protection law can be enhanced to better reduce false or misleading sustainability claims (greenwashing) by providing greater certainty and clarity with regards to these claims. (267 words)

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1. Introduction

Sustainable development, defined as “development that meets the needs of the present without compromising the ability of future generations to meet their own needs,” comprises economic, social and environmental components (United Nations [UN], n.d.).

The private sector is seen as an essential component in achieving environmental sustainability. Sustainable development would require producers to responsibly utilise finite resources to protect future generations. Firms can also be part of the “green economy”¹ or employ environmentally sustainable processes to reduce environmental damage (Portney, 2015). The UN has also emphasised the role of businesses as part of the Sustainable Development Goals (SDG) (UN, n.d., SDG 12.6). With the private sector playing a critical role in sustainability, it is important to analyse how competition and consumer protection can affect sustainability efforts, as key elements of private initiatives.

To explore how competition and consumer protection can improve sustainability, this essay will analyse the various causes of market failure in the market for sustainable products and initiatives: demand-side market failure arising from information asymmetry and positive externalities, as well as supply-side failure due to first-mover disadvantage. Competition law and consumer protection law have the potential to correct the sources of market failure, thereby supporting environmental sustainability in Singapore.

¹ A sector in the economy that focuses on environmental protection.

2 Market Failure

Environmental sustainability necessitates productive and dynamic efficiency, such as better methods of production that reduce the use of raw materials or more efficient use of recycled components (OECD, 2020). Competition among firms can enhance productive efficiency and innovation of energy-efficient technology (Vickers, 1995; Malinauskaite, 2022).

Furthermore, with the increasing awareness of climate change and greater willingness to be more sustainable (National Climate Change Secretariat [NCCS], 2019), many consumers prefer sustainable products, with increasing demand for sustainable products (Gershoff & Frels, 2014), viewing it as part of product quality (Volpin, 2020), thus sustainability as an element of product differentiation could also incentivise firms to compete to innovate based on environmental considerations.

However, in reality, market failure may occur, preventing the free market from providing the full possible extent of sustainability benefits. This includes demand-side market failure due to information asymmetry and positive externalities, along with supply-side market failure caused by first-mover disadvantage.

2.1 Demand-Side Market Failure

Even though consumers may value sustainability, they may be unable to make sustainable decisions due to information asymmetry and positive externalities.

Information asymmetry whereby firms have more information than consumers about how sustainable their products are can result in market failure. This provides the opportunity for firms to “greenwash” their products with misleading claims of sustainability, with 40% of firms engaging in this practice globally (Competition and Markets Authority [CMA], 2021). Consumers are also

unable to adequately interpret carbon data (Thøgersen, 2021), exacerbating this issue. Not only does this cause consumers to underestimate the environmental impact of unsustainable products marketed as “green” (Alves, 2009), greenwashing reduces investor and consumer confidence in legitimate environmentally sustainable companies, reducing demand thereby weakening the market for sustainable goods and services (Delmas & Burbano, 2011).

Market failure also occurs due to positive externalities, where consumers are unwilling to pay for the wider benefits accruing to society when purchasing sustainable products. Lowering carbon emissions due to sustainable purchases reduces the impact of climate change, generating a myriad of external benefits such as improved air quality and public health.

2.2 Supply-side Market Failure

There is a “first-mover disadvantage”, whereby firms fear a costly investment in sustainable practices or technology would lead to competitive disadvantage when competitors undercut them by using cheaper unsustainable methods of production (International Chamber of Commerce [ICC], 2020). As firms reduce sustainable efforts, an underproduction of sustainable initiatives occurs, resulting in a sub-optimal output level.

2.3 Impacts and solutions

As a result of market failure, there is an underallocation of resources to the production of sustainable goods and initiatives, leading to welfare loss to the society.

Demand-side causes of market failure can be targeted with regulations that correct information asymmetry and aid consumers’ decision-making process when purchasing sustainable products.

To overcome supply-side causes of market failure, collaboration among firms (vertical and horizontal) is needed to reduce the uncertainty and first-mover disadvantage, to increase sustainable initiatives by firms.

Furthermore, there are significant environmental benefits to be reaped from collaboration as significant reduction of greenhouse gases (“GHG”) production can be achieved through more efficient use of existing capacity via resource sharing and collective logistics organisation (Scott, 2016). The use of public goods as an input also necessitates agreements to ensure controlled use of finite resources (Scott, 2016).

3 Role of Competition Law in driving sustainability

Competition law can promote sustainability by preventing abuse of dominance and ‘greenwashing’. On the other hand, collaboration among firms such as self-regulation, the exchange of technical information, and restriction of production of unsustainable goods to promote sustainability, could potentially constitute anti-competitive behaviour, giving rise to tension between sustainability and competition law.

Positive externalities arising from sustainable efforts should be taken into account as economic efficiencies to be weighed against their anticompetitive effects. These externalities can be measured with established methods such as shadow pricing.

3.1 Competition Law to protect sustainable developments

Since competition can enhance productive and dynamic efficiency, which are necessary elements in achieving sustainability, conventional applications of competition law can promote sustainability as a secondary effect. For instance, the European Commission (“EC”) is investigating Public Power Corporation (“PPC”) in the Greek wholesale electricity market, which

holds over 67% of the market share, for potential abuse of their dominant position. The EC was concerned that PPC's predatory bidding behaviour was anti-competitive, impeding rivals from competing in the electricity market, which might have hampered investments in more sustainable forms of energy (EC, 2021). Therefore, competition law could encourage investment in alternative methods of production and products, which are potentially more sustainable.

Competition law could also prevent firms from engaging in anti-competitive agreements and cartelising while using sustainability as a front, sometimes referred to as greenwashing (Malinauskaite, 2022). To illustrate, Daimler, BMW, Volkswagen, Porsche and Audi initially cooperated to develop more sustainable diesel vehicle systems by holding technical meetings, which improved consumer welfare and the environment (EC, 2021). However, this evolved into collusion among the five firms to evade competition on this more sustainable technology and go beyond European emission standards (EC, 2021). The EC's fine of €875 million for the firms' anti-competitive agreements thus drove sustainability by promoting competition on more sustainable vehicle systems.

Singapore's Competition Act 2004 ("the Act") which prohibits anti-competitive agreements ("Section 34 prohibition"), and abuse of dominance ("Section 46 prohibition") can play an analogous role in promoting sustainability in similar cases.

3.2 Conflict between Competition Law and Sustainability

Many joint sustainable initiatives are unlikely to infringe competition laws since collaborative efforts such as joint research are unlikely to substantially restrict competition and are excluded from Section 34 in the CCCS Guidelines (CCCS, 2022).

However, competition law might nevertheless act as an obstacle to some sustainable initiatives. Firms may breach the Section 34 prohibition if such efforts involve firms reducing production of unsustainable goods, sharing of potentially sensitive information to reduce unsustainable production methods or setting industry standards that go beyond state requirements. For instance, a private initiative among firms such as setting sustainability standards², particularly relevant for resource-intensive product markets (Scott, 2016): a green label can have pro-competitive effects of improving product quality, distribution, and consumer access to sustainability information, which contributes to the growth of the market for sustainable goods (EC, 2022). Despite its benefits, this may violate the Section 34 prohibition by possibly raising entry barriers, therefore restricting competition.

Competition law as an impediment to sustainable efforts from firms could be exacerbated by legal uncertainty surrounding such collaborations. Even though Section 41 of the Act exempts agreements that i) improve production and distribution; or ii) promote technical or economic progress from the Section 34 prohibition (with caveats), there has been no explicit reference to environmental benefits in guidelines nor precedent cases related to sustainability and competition in Singapore for firms to ascertain if their sustainability efforts would violate the Act. This legal uncertainty could cause hesitation to pursue sustainable collaborations. However, this concern is less significant in Singapore where unlike some countries, businesses can seek guidance from the Competition and Consumer Commission of Singapore (“CCCS”) if in doubt.

² According to the European Union’s Guidelines on Horizontal Co-operations, sustainability standards are based on sustainability parameters (e.g., environmental impact). They differ from technical standards in that they do not specify a particular production method or technology used. Many are process, management or performance based.

3.3 Balance between Competition and Sustainability – should environmental benefits be considered as economic efficiencies?

Sustainable initiatives generally lower emissions compared to alternatives, therefore generating positive externalities since consumers and firms benefit from higher quality of the environment (Perrings & Kinzig, 2021). This should be considered when discussing their effects on competition. Considering that the carbon tax was introduced to reduce negative externalities of carbon-emitting production processes, some anti-competitive effects of sustainability agreements could be similarly viewed as the cost of positive externalities (economic efficiencies), provided that these benefits outweigh the cost of anti-competitive effects.

These efficiencies are acknowledged in various jurisdictions: the EC has provided guidelines that allow sustainability agreements with anti-competitive effects under Article 101(3) of the Treaty on the Functioning of the European Union (“TFEU”), if conditions are met; and the CMA has also specified that sustainability agreements could provide benefits that exceed the possible cost of reducing competition. This could be similarly applied to Singapore, where Section 41 of the Act provides exemptions based on ‘net economic benefits,’ that environmental benefits could fall under.

In fact, Singapore could exempt sustainable efforts under Section 41 more directly since she maintains a total welfare approach compared to other jurisdictions such as the European Union (EU) and United Kingdom (UK) that aims to maximise consumer welfare (Toh, 2018). Even though sustainable efforts could raise price and/or lower product variety for consumers, it may still align with the total welfare approach if it raises societal welfare in the form of environmental benefits. In comparison, exemption under Article 101(3) of the TFEU requires agreements to provide consumers “a fair share of the resulting benefits”, which if interpreted to mean lower prices, could hinder sustainability efforts. Thus, exempting anti-competitive agreements that

promote sustainability from the Section 37 prohibition would be consistent with Singapore's approach to sustainable law and could be more feasibly implemented.

3.3.1 Measuring externalities of sustainable initiatives

In order to weigh the costs and benefits of allowing anti-competitive sustainability agreements, there is a need to measure the externalities of such agreements.

There are established methods of quantifying the externalities of sustainability agreements used by competition authorities in various jurisdictions, such as shadow pricing. Shadow pricing involves assigning a hypothetical value to an externality (Stiglitz et al., 2017), such as shadow pricing on carbon. This method was applied in 2013 by the Netherlands Authority for Consumers and Markets ("ACM") – which accepts "environmental benefits" as benefits that consumers enjoy under Article 101(3) of the TFEU that exempts anti-competitive agreements – to measure the emissions reductions of a supposed sustainability agreement among several energy producers to determine whether the benefits offered outweighs the anti-competitive effects of the agreement (ACM, 2013).

The shadow carbon price differs based on the state of the economy, environmental goals of the country and various assumptions made when calculating the carbon price such as the ability of the economy to reallocate resources and adopt carbon-efficient technologies (Stiglitz et al., 2017). To limit global warming below 2°C, the target set by the Paris Agreement, the shadow price of carbon increases each year with estimates ranging from US\$15 to US\$360 per ton in 2030, and US\$45 to US\$1,000 in 2050 (Stiglitz et al., 2017).

Once the potential reduction in GHGs is priced, this can be compared to the impact of reduction of competition – such as price, productivity and innovation among other indicators

(OECD, 2021) – to determine whether the benefits of allowing anti-competitive sustainability agreements exceed the costs.

4. Consumer protection and greenwashing

Greenwashing with misleading claims relating to the sustainability of a product can be covered under the Consumer Protection (Fair Trading) Act (“CPFTA”). The CPFTA protects consumers against unfair practices including false or misleading claims or exploiting consumers' inability to understand the nature and impact of the transaction, in which case the consumer has the right to sue the business.

However, as established in Section 2.1.1, consumers are often unable to interpret carbon data, and are therefore unable to accurately ascertain whether a firm has engaged in greenwashing, reducing the effectiveness of the CPFTA. Furthermore, there is also uncertainty surrounding the CPFTA's application to sustainability claims due to the lack of guidance with regards to greenwashing.

Greenwashing can be reduced with more stringent regulations that specifically apply to sustainability claims, similar to the Green Claims Code introduced by the CMA. Stricter rules should include presenting green claims in an accurate and direct manner that does not exclude crucial data and is easily accessible to consumers, correcting information asymmetry. The existence of regulations specific to sustainability claims also allows consumers to determine violations with greater ease and certainty, aiding the enforcement against greenwashing.

The reduction of greenwashing can prevent unsustainable firms from using false sustainability claims to introduce price premiums, enhancing the reliability and credibility of

legitimate sustainable firms which can encourage greater investment and consumption of sustainable products, strengthening the market for these goods.

5. Conclusion

As the climate crisis worsens, the costs incurred will likely mount, presenting a greater impetus to facilitate any measures that alleviate the impacts of climate change such as strengthening the market for sustainable products.

Existing sources of market failure in the market for sustainable goods and services can be minimised with competition and consumer protection regulations. Collaborative efforts between firms which are key to promoting environmental sustainability can be enhanced with greater legal certainty surrounding such collaborations, particularly with regards to considering environmental benefits as economic efficiencies that exempt firms from the Section 34 prohibition. Information asymmetry can be further reduced with explicit regulations concerning greenwashing. (2339 words)

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