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Competition in the Circular Economy – Note by Latvia

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More documents related to this discussion can be found at
<https://www.oecd.org/competition/competition-in-the-circular-economy.htm>

Antonio CAPOBIANCO
Antonio.Capobianco@oecd.org, +(33-1) 45 24 98 08

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Latvia

1. General competition legal framework

1. The current legal framework of the competition law in Latvia allows the competition authority to consider circular economy principles during the assessment. In its evaluation of the competitive situation in the relevant market, the competition authority may examine efficiency factors and their impact on the competitive situation in the relevant market and other related markets. The competition on the market and the efficiency factors interacts in many different ways, they are related to resource efficiency as well as other elements related to the circular economy.

2. The CC has not encountered any significant conflict between the objectives of competition law and the underlying conceptual foundations of the circular economy. When it comes to situations of potential conflict, the CC has always taken the position that restrictions on competition or changes in market structure can only be justified on the basis of economically justified long-term efficiency gains for society and the economy.

3. In order to clarify and assess the considerations of the circular economy in relation to changes in the market structure and competitive situation in the municipal waste management market, the CC conducted a consumer survey (Study) to seek and analyse the views of individuals on the possible change in the market structure (from a competition on the market to a competition for the market) in this particular market in Riga. The CC applied the findings of the study to a case concerning the municipal waste management model planned and concluded by the Riga City Municipality under a concession agreement (the Concession Agreement).¹ The planned management model envisaged a change in the municipal waste management services in the City of Riga resulting into a 20-year long monopoly in the market starting in 2019 (see Section B, Case 1 for more information on this case and the CC's decision of 09.09.2019 on an interim solution).

4. According to the results of the Study, waste producers in Riga preferred to freely choose their waste management provider. This market model existed in the municipal waste management market in the territory of Riga City until 2019. According to the findings of the Study, since the change in the market structure, the waste producers (both natural and legal persons) encounter various inconveniences that could be avoided if the waste producers were given the possibility to freely choose the waste management service provider and if the service providers were exposed to competition pressure.

5. The results of the study indicated that the current situation with each waste operator providing services in an exclusive service area is difficult to reconcile with the general interests and needs of waste producers (holders), which were better addressed and solved when waste management service providers were in competition with each other.

6. The conclusions reached in the Interim Decision regarding the impact on competition and the market situation after conclusion of the Concession Agreement were reinforced by the results of the Study. According to the results of the Study, the outcome of the Concession Contract is not only harming the competition and market participants not

¹ The CC decision on interim measures available in Latvian: https://lemumi.kp.gov.lv/files/documents/20190909_KP_Interim%20measures.pdf

involved in the Concession Contract, but also negatively affects the customers i.e., waste producers.

2. Case experience

7. Competition law should not be considered as an obstacle to the initiative and development of a circular economy. Collective initiatives by market participants, including those relating to the circular economy, could be assessed as an agreement or merger. Given the above, during the merger review process, the CC assesses not only the effects of the merger on competition, but also the efficiencies of the proposed merger (the circular economy-related efficiencies in the merger case as described below). When assessing agreements between market participants, such agreements are considered valid if they contribute to the improvement of the production or marketing of goods or to economic development to the benefit of consumers and (1) do not impose restrictions which are not necessary to achieve the objectives; (2) do not have the potential to eliminate competition in a substantial part of the relevant market.² Consequently, market participants are not deterred from taking the initiative to participate in collective initiatives in the circular economy, provided that no restrictions are imposed on market participants which are not necessary to achieve the objectives of the circular economy and competition is not eliminated in a substantial part of the market. Thus, before entering into an agreement on cooperation to achieve common objectives of the circular economy, the CC invites market players to consult the CC to prevent potential distortion of competition. The CC will consider whether the agreement restricts other market participants (operating in the same relevant market and/or a related relevant market) to compete as well as the general competitive situation in the relevant and/or related markets.

8. In the following paragraphs the CC provides details of investigations examining changes in market structure, the competitive situation and the (expected) impact of these changes on market participants, economic benefits for consumers and efficiency. In the Case 1, the CC assessed the potential effects of a change in market structure on competition, the expected emergence of a dominant position in the relevant market over a sustained period and concluded that the change in market structure did not lead to any economic benefits. In its Decision of 28.11.2022 concerning the acquisition of decisive influence by AS CleanR Grupa over SIA RSC Noma (Case 2), the CC evaluated the impact of the merger on the competitive situation and concluded that the merger would increase customer benefits and facilitate the implementation of circular economy principles.³

9. The evidence in Case 2 suggested that the most relevant determinants of the future competitiveness of undertakings are not their historical market shares, but rather their existing sorting and recycling capacity and their technological capacity (the intensity and efficiency of its use). Consequently, the investigation of the case addressed the circular economy aspects (on-site sorting of materials, on-site preparation for recycling or separate site preparation for recycling and/or reuse of construction waste) and their impact on the future competitive situation in the construction waste management market. Accordingly, in Case 2 the CC analysed whether the market participants have unused and available capacity

² Section 2 of Article 11 of Competition Law. Available in English: <https://likumi.lv/ta/en/en/id/54890-competition-law>

³ The CC decision available in Latvian: https://lemumi.kp.gov.lv/files/documents/20221128_L%C4%93mums_CleanR_publickojam%C4%81%20versija_Nr.21.pdf

that would allow them to increase their offer oriented towards the circular economy in the relevant market and thereby compete successfully with the merged undertaking.

10. In Case 2, the CC assessed the ability of market participants to offer on-site construction waste sorting services and the ability/potential ability of waste management operators to offer a construction waste management service to customers in the future that would ensure compliance with circular economy principles, i.e. the ability of waste management operators to offer a construction waste management service that would include the preparation and recycling of construction waste. Such a service is considered to be part of the efficiency considerations. This can be regarded as a contribution to the market offer, development and as implementation of circular economy principles in the waste management activities. The CC cleared the merger in question because the investigation revealed that there were already operators in the relevant market that could offer on-site sorting of construction waste management. Similarly, companies already providing construction waste management services are seeking to increase their capacity in the construction waste management market. The merged company identified a number of efficiencies from the merger, such as increased availability of the construction waste management service to customers. This business model can therefore be characterised as an efficient use of resources in line with the principles of the circular economy.

3. Advocacy

11. The CC examines the legislation drafted by the Ministries and issues opinions within the scope of its competence. The Ministry of Environmental Protection and Regional Development (the Ministry), which develops the regulatory framework, including the waste management sector, is responsible for environmental protection and waste management policy in Latvia. The waste management regulatory framework contains conditions for the development and operation of the circular economy and applies the principles to the waste management sector as well as to the management of specific types of waste. The CC takes into account both the aspects and efficiency criteria for the successful development of the circular economy and the conditions for ensuring fair competition when issuing its opinion on the draft legislation. If any interested party proposes changes to the regulatory framework, and these changes may affect market structure or other factors affecting competition, the CC may propose to carry out an economic analysis that should determine whether and how the proposed changes will alter the competitive situation. Based on this economic analysis, the parties will determine whether the proposed amendments that may change the market structure or otherwise affect the competitive situation are proportional i.e., if they are the only and most effective way to ensure the implementation of the principles of the circular economy and the achievement of environmental objectives. Below the CC provides information on its interaction with policy makers in relation to circular economy legislation or regulation specific to the waste management sector (regarding re-use, recycling).

12. In 2023, amendments to the Waste Management Law came into force,⁴ allowing retailers who generate at least 20 tonnes of packaging waste per month at their place of business to hand over the packaging waste generated at that place to a recycler. This allows waste producers to transport the waste to a common delivery and collection point before

⁴ Waste Management Law. Available in English: <https://likumi.lv/ta/en/en/id/221378-waste-management-law> depoziņa

transferring the packaging waste for recycling. In this way, waste producers (retailers) are given the possibility to transfer packaging to a waste manager of their choice.

13. This amendment: 1) enables recyclers of packaging waste to receive the highest quality recyclable material. It should be noted that the recyclable material is delivered to the recyclers using fewer delivery stages, thus reducing the consumption of various resources (fuel, machinery, labour, etc.); 2) use of reverse logistics. Reverse logistics ensures that the principles of the circular economy are implemented in the most efficient way possible.

14. From 01.02.2022, Latvia operates a deposit system,⁵ comprising beverage packaging collection from end-users, including sorting, transport, storage, recycling or preparation for re-use in accordance with its original purpose, as well as the planning and organisation of these activities.

15. Prior to the introduction of the deposit system, the Ministry of Environmental Protection and Regional Development developed a regulatory framework for the introduction and operation of the deposit system in Latvia. The CC cooperated with the Ministry and provided its assessment on the establishment of the deposit packaging management system and the criteria for the selection of the deposit packaging management operator.

16. The legal framework provided for the creation of a single deposit scheme operator, and the CC indicated that before the Deposit System is established, an impact assessment of the system should be carried out, including an assessment of several possible models for the implementation of the Deposit System and their operational impact on: 1) consumers and 2) other specific markets that could potentially be affected by the introduction of the Deposit System. Such an assessment allows for greater certainty on several important aspects, including: (1) whether the operation of the Deposit Scheme will be most efficiently ensured on the market by one or more operators competing with each other and (2) whether the proposed Deposit Scheme model is the most optimal in terms of, for example, cost-effectiveness, etc.

17. In case several undertakings apply for the position as a deposit scheme operator, the CC suggested that taking into account the principles of circular economy, the undertaking should be selected based on efficiency criteria, such as cost per unit managed, deposit packaging management fee, location of collection points, coverage, etc., in order to achieve the required objectives with the least resource consumption. The main criterion for evaluating applicants therefore is the 'plan for organising and implementing the operation of the deposit scheme' (efficiency criterion).

18. After carrying out an assessment of the functioning of the Deposit System, the CC concluded that the Deposit System will be most efficiently operated by a single operator, which will thus hold a dominant (monopoly) position in the management of deposit packaging in Latvia.

19. In 2021, the CC completed its monitoring of the glass packaging waste management market.⁶ Packaging waste is collected by municipal waste managers, who conclude contracts with producer responsibility scheme (PRS) operators for the collection of packaging waste from households ('end-users'). PRS operators are required to ensure: 1)

⁵ See Chapter III of Packaging Law. Available in English: <https://likumi.lv/ta/en/en/id/57207-packaging-law>

⁶ Available in Latvian: <https://www.kp.gov.lv/lv/media/9236/download>

collection of packaging waste throughout the territory of Latvia, 2) transport the collected packaging waste for recycling and recovery, recycling or recovery.

20. The CC concluded that the barriers to entry for operators entering the market for the management of packaging waste are not significant, but that the requirements to operate successfully and continuously on the market are considered significant. At the same time, it appears that there are high barriers to the entry and operate for individual management systems, as there have been no individual management systems on the packaging waste management market in Latvia since 2016. The CC concluded that entry of new operators in the glass packaging management market may be easier than a long-term presence.

21. Although there are new entrants in the market for packaging waste management, the PRS operators often leave the market after relatively short period of time (1-3 years), indicating that it might be difficult for them to comply with the regulatory requirements to operate in packaging waste management market, including glass packaging. Recycling capacity for packaging waste in Latvia is currently weak and most of the collected packaging waste (including glass) has to be exported to other countries for recycling. This increases the "cost" of the service provided by PRS operators i.e. the cost of delivering the collected packaging waste to the recycling facilities increases significantly. New entrants initially have a small number of contracted partners (packagers), hence the total amount of management fees received is small compared to RSO operators with a longer presence on the market and with several hundred (or thousands) of contracted partners. Consequently, new entrants may have to cover these costs from revenues other than the packaging management fee paid by packagers.

22. After the analysis on the competitive situation on the glass packaging management market, the CC concluded that the market has a long-standing oligopolistic market structure (two market players (packaging waste operators / PRS operators) who has a combined market share of more than 90%). New entrants (packaging waste operators/PRS operators) are able to enter the market, but after 1-3 years they exit. This indicates that new entrants are able to overcome barriers to entry but are not able to operate in the market on a sustained basis. One of the reasons for new entrants to exit after 1-3 years is the lack of customer interoperability, i.e. new entrants need to attract as many customers as possible to be successful in the market. If the number of customers remains stable or decreases after 1-3 years of operation, the new entrant's performance on the market is hampered and they exit the market. This conclusion was drawn by the CC in the context of the monitoring of the market for glass packaging management which analysed the characteristics of the relevant market. The CC concluded that customers ('packagers') enter into a contract with a new entrant for a period not exceeding 3 years. At the end of the contract, the customers ('packagers') enter into a contract with a long-standing player on the market, thus returning to the previous service provider ('packaging waste operator'), who has been active on the market for a long time. This behaviour of customers may be seen as a need for assurance and stability, and that the packaging placed on the market by the customers will be responsibly managed and recycled to the required volume and quality.

23. Each packaging type is considered as a homogeneous product i.e., plastic, cardboard, glass, metal. The market is characterised as a transparent market, where the products are homogeneous, prices are publicly available, and it is relatively easy and timely monitored by competitors. At the same time the packaging waste management is considered to be an oligopolistic market, where one can normally assess and predict to a certain degree the actions of potential competitors, for instance, how a competitor will behave and react to its actions.

24. To ensure that the principles of the circular economy are implemented in practice, the legislators set increasingly stringent standards for the recycling of packaging waste,

separation of recycling materials and requirements for recycling. The higher volume of collection and recycling increases the costs for producers, which further influences the waste management fees charged. The amount of fee is considered as the only criterion for differentiating the service provided by each PRS operators to its contractual partners. Based on the above, the management fees charged by PRS operators are expected to increase in the future.

25. The CC continuously monitors legislative and regulatory acts regulating waste management activities. Further, the CC gives its opinion on the regulatory provisions on waste management, which contain conditions related to the possibilities of operators to provide waste management services in general or to provide certain activities within the framework of waste management. The CC's position was taken into account in the process of drafting the legislation.

26. According to the Waste Management Law, in order for a waste manager to obtain a permit to carry out waste management activities, it must prove that it has sufficient financial security. It is used to cover costs in cases where the waste manager has failed to carry out the necessary waste operations.⁷

27. After assessing this requirement, the CC pointed out the necessity for principles of proportionality and progressivity when determining the amount of the financial guarantee that the waste management operator should maintain, i.e. the higher the volume to be managed (recycled), the higher the amount of the financial guarantee. Without setting the volume of waste to be managed (recycled) as a benchmark for determining the financial security: (i) operators (recyclers) who have received permits for operations with relatively small volumes of waste are subject to a relatively higher financial burden than operators (recyclers) who are allowed to manage (recycle) several times the volume of waste; (ii) it creates an uneven playing field in the market.

28. The CC used similar approach when it assessed the financial and administrative requirements for wood packaging recyclers. In the view of the CC, the requirements set out in the draft regulatory framework: 1) were disproportionate to the potential environmental damage caused by their activities and 2) created significant barriers to new entrants in the wood packaging recycling market, thus hindering the competition. Noteworthy, the CC pointed out that the amount of financial guarantee is based solely on the condition that the issued permit covered municipal or hazardous waste management. Instead, the financial guarantee should reflect, inter alia, the volume and type of waste to be managed and the environmental impact assessment of the waste operations carried out by the operator.

29. According to the idea proposed by the Ministry of Environmental Protection and Regional Development, a single PRS operator would make more efficient use of resources and simplify the logistics system. In 2021, the CC made an assessment of the planned changes, and pointed out that in order to establish that resource efficiency can be achieved with a single PRS operator, it is necessary to carry out an analysis on economic performance of a different number of PRS operators. When multiple PRS operators are active on the market, they operate in a competitive environment, and offer their existing and potential customers a higher quality service at the lowest possible price. In the view of the CC, the Report did not lead to the conclusion that in order to ensure efficient resource management, only one PRS operator should be allowed to carry out the activity. The CC considers that when changing the management model, it is necessary to assess the risk of restriction of competition (including exclusion of competition) in a market where

⁷ Section 1⁴ of Article 12 of Waste management Law. Available in English: <https://likumi.lv/ta/en/en/id/221378-waste-management-law>

competitive conditions currently exist. In addition, a number of possible management models need to be evaluated and compared in order to reach a conclusion on the most appropriate model for Latvia for the management of all types of tyres. In this way, the principles of the circular economy and the choice of management model would be balanced simultaneously, even if it requires to make the change the market structure.

30. As a result, the CC concludes that the weaknesses in the tyre management system are due to gaps in the regulatory framework and insufficient control and supervision. One of the risks of the current tyre management model, is the structure of the scrap tyre management fee, as well as its application and review mechanism. The cost of recycling scrap tyres has a significant impact on the management fee, the environment and the achievement of circular economy objectives.