

Finding Collective Dominance in an *ex ante* environment

- **Draft European Electronics Communications Code places more emphasis on collective dominance.**
- ***Ex post* conditions well known, but how should an NRA find collective dominance *ex ante*?**
- **Guidance is needed to ensure focus on structural market conditions and the supporting role of behaviour**

One of the many competition problems being considered in the draft European Electronic Communications Code (EECC) is Collective (or Joint) Dominance: a situation where two or more firms constitute a collective entity vis-à-vis their competitors, trading partners and suppliersⁱ. The situation is of concern to the European Union now because of what it sees as a risk of oligopoly markets, particularly in relation to wholesale local access where a cable operator competes with the fixed line incumbent. This edition of Hexagon examines the economic structural conditions that may need to be considered for a finding of Collective Dominance *ex ante*.

The European Commission's draft text of Recital 175 of the EECC suggests that where there are two operators, at least one of which offers wholesale access on reasonable commercial terms such that retail markets can be sustainably competitive, "national regulatory authorities are unlikely to need to impose or maintain SMPⁱⁱ based wholesale access obligations". It further states that where three operators are present, NRAs "will be less

likely to identify an operator as having SMP, unless they make a finding of collective dominance".

The structural conditions in which a single firm may be found to have SMP *ex ante* are well known. They start with the firm's market share and include factors such as countervailing buyer power, barriers to entry and so forth. Crucially, all these factors concern the *structure* of the market and not the *behaviour* of the firm that may have SMP.

The jurisprudence on collective dominance is based on competition law and tends to concern the behaviour of firms. In *Compagnie Maritime Belge* firms are found to be collectively dominant if they adopt a uniform conduct or common policy in the marketⁱⁱⁱ. Any examination of behaviour is necessarily *ex post*, as the NRA would have to look back and see what firms have actually done rather than what they have the potential to do.

The most referenced case in relation to *ex ante* collective dominance is *Airtours*: a merger



between two UK based charter airlines. Although under competition law, any merger case is *ex ante* as it considers how the merged entity could behave in the post-merger market structure.

Airtours establishes a three-step procedure for a finding of collective dominance:

- i. Transparency: the ability to monitor that other firms are abiding by a common policy;
- ii. An incentive not to depart from the common policy and a means by which a dissenter can be punished; and
- iii. Foreseeable reaction of competitors and consumers would not jeopardise results of common policy.^{iv}

The structural conditions under which these steps may occur are reasonably well known, at least in principle. They require that there are few firms in the market, each with similar and stable market shares, and incumbents are protected from future competition by high barriers to entry.

An NRA considering whether a market may be subject to collective dominance needs to operationalise this process. As with single firm SMP, it may start with the combined market share of the potentially dominant firms, but what level of market share should raise concerns?

There is some guidance in jurisprudence. *Gencor* suggests that the duopoly share should exceed 50% and *Compagnie Maritime Belge* suggests the combined share should exceed the presumed dominance threshold, which also implies 50%. On this criterion just about all mobile markets and most wholesale broadband markets would pass the threshold at which collective dominance should be considered.

Market shares, however, are only ever an initial indicator of dominance and other criteria must be taken into consideration. In relation to market shares, the NRA may wish to consider both the symmetry and stability of market shares over time. If the two firms each have around 25% - 30% share and have had for some time, is that more likely to result in collective

dominance than if one has 35% and the other 15% and these shares have fluctuated over time?

There is not time here to consider all the other factors that may confer market power. However, some questions could be asked.

First, countervailing buyer power is an important constraint on a potentially dominant firm. If the customer has a credible alternative supplier, then the potentially dominant firm will find it harder to exploit that position. Where there are at least two firms of a reasonable size, can the consumer be said not to have buyer power? If neither firm has an incentive to depart from a common policy, perhaps there is no countervailing buyer power as the firms could be said to constitute a collective entity. However, can we observe whether there is a common policy just by looking at the structure of the market and not the behaviour of firms in the market?

Secondly, barriers to entry allow firms in the market a quieter life as they are unlikely to be

challenged by new entrants. If there are at least two firms in the market each with a strong position, it must be the case that barriers to entry were lower than if there is just one firm. An NRA can assess whether there are structural barriers that would prevent further market entry and so confer collective dominance on incumbents.

Thirdly, single firm SMP can be conferred by that firm having access to an essential facility that others cannot duplicate economically. Can this structural feature apply in a market with several suppliers?

Finally, the draft text of Recital 175 refers to the need for only one of the two network operators to be offering commercial wholesale access for the NRA to be unlikely to need to impose SMP obligations. This would mean that the sole firm that does offer wholesale access would be under an “indirect constraint” from the firm that does not.

Briefly, an indirect constraint means that a monopolist at wholesale level cannot raise

prices above the competitive level because the subsequent rises in retail prices by its downstream customers would lead to a high level of switching to its rival that does not offer wholesale access. The resultant loss of sales would mean that any such price rise would be unprofitable, *provided that the rival does not also raise prices.*

The question again arises as to whether the presence of indirect constraints can be observed from the structure of the market or whether an NRA would have to look more closely at the behaviour of firms in the market and whether they adopt a common policy.

One structural feature that would provide information for the NRA is the degree of competition between wholesale customers of the access provider. If competition is strong they are more likely to have competed retail profits away and so have to pass on any wholesale price rise to customers. This would strengthen the indirect constraint. If competition is weak, then at least some of the

wholesale customers would be able to absorb the price rise, weakening indirect constraints.

The degree of competition however is only a proxy measure for profitability and the NRA would really have to analyse the actual level of profits earned.

Overall, establishing whether firms may have collective dominance in a market is harder to establish *ex ante* than single dominance. Some of the structural indicators of single dominance are less likely to apply and a closer examination of behaviour will be needed to assess whether firms stick to a common policy. Clear guidance will be needed as to the structural indicators of collective dominance and where a behavioural assessment may play a supporting role.

ⁱ Stenborg, M. (2004). Forest for the Trees: Economics of Joint Dominance. *European Journal of Law and Economics*, 18(3), 365-385.

ⁱⁱ Significant Market Power

ⁱⁱⁱ Stenborg (op cit)

^{iv} BEREC Report on Oligopoly Analysis and Regulation November 2015

