

# A Brief Discussion of “Martin Hellwig: Competition Policy and Sector-Specific Regulation for Network Industries”

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[Views personal. Not necessarily those of the OFT]

# Three key messages of the paper

1. Common costs in network industries present problems for competition policy (and regulation)
2. Competition policy is not well suited to certain tasks such as access regulation
3. The interaction of regulation and competition policy requires careful institutional design

# 1. The Common Cost Problem

- ▶ How to prevent excessive pricing and/or exclusionary pricing by a multi-product firm with:
  - ▶ Pockets of monopoly power alongside pockets of competition
  - ▶ Common costs across products, such that:
    - ▶ Setting prices = stand-alone costs can imply excess profits over system
    - ▶ Setting prices = incremental costs can imply losses over system
  - ▶ Network effects, such that:
    - ▶ Incremental revenue from a given sale can exceed price

# Individual versus system prices

- ▶ Hard to assess individual prices without analysis of pricing over the system:
  - ▶ The 'waterbed' issue
  - ▶ Bundeskartellamt experience
- ▶ But competition law does not dictate assessment of individual prices only:
  - ▶ E.g. OFT assessment of BSkyB margin squeeze – all channels contribute to recovery of the cost of set top boxes and thus BSkyB's downstream margin was assessed across all product lines.

# Why system competition is not enough

- ▶ Imperfect competition means rents are not completely dissipated
- ▶ Purchasing decisions can be distorted:
  - ▶ excessive consumption of one element, e.g. handsets, and insufficient consumption of another element, e.g. off-network calls
  - ▶ cross subsidy from outside the system e.g. fixed line users subsidising mobile users
- ▶ Exclusionary behaviour can still occur
  - ▶ e.g. Napp (OFT, 2001)

## 2. Problems with using competition policy to regulate access

- ▶ *Ex post*, not *ex ante*? Need to observe a problem before can use competition law to fix it
- ▶ Insufficient information?
- ▶ Common cost issue?

# The Common Cost Issue in Antitrust

- ▶ True that competition policy struggles where there are common costs
  - ▶ Key is test employed for abuse of dominance – How high is the bar for intervention? US v EU. ‘form-based’ vs ‘economic’. Should ‘first mover advantages’ be removed when applying the ‘efficient’ competitor test?
- ▶ Arguably competition policy better at preventing enhancement/protection of dominance than at actively promoting competition.
- ▶ But problem may be lessened if employ *long run* incremental costs as relevant cost measure:
  - ▶ E.g. as employed by Ofcom in Freeserve II

### 3. Institutional design

- ▶ Need for coordination between sector-specific regulators and competition agencies, due to:
  - ▶ Information problems (and 'waterbed' problems)
  - ▶ Market definition can be haphazard or subject to political influence
- ▶ Economically sound and legally well established methodologies for market definition do exist, although may be misapplied
- ▶ UK model gives sector-specific regulators concurrent powers for competition law enforcement. Information obtained and considered within relevant context

## Market definition: A brief comment

- ▶ Concern: market definition can be haphazard or subject to political influence
- ▶ But: EC adoption of narrow markets for network specific mobile termination makes sense
- ▶ Relevant market definition for long distance calls would seem to depend upon how the consumer chooses the long distance carrier and how firms compete