



Federal Network Agency for Electricity, Gas, Telecommunications, Post and Railways

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**Price squeeze tests in electronic communications
– The German Approach –**

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Introduction

- Under section 28 of the German Telecommunications Act, dominant companies are generally not allowed to substantially affect the competitiveness of other undertakings in a telecommunications market
- Abuse of this kind is presumed for instance in the case of a price squeeze
- The current practice of determining the conditions under which a margin squeeze exists raises a number of questions



Main questions

1. What perspective should be used as a basis for a price squeeze test in the context of sector-specific regulation (a reasonably efficient alternative operator or the dominant firm)?
2. What is meant by the term “efficient competitor”?
3. What approach should be taken to determine efficient costs?
4. Should price squeeze tests be performed per service or per basket of services?



Legal requirements

- Under section 28 of the German Telecommunications Act, abuse is presumed, if

“the margin between the price the SMP public telecommunications operator charges competitors for an access service or facility and the corresponding retail price is not enough to enable an efficient undertaking to achieve a reasonable return on capital employed in the retail market.”



What perspective should be used as a basis for a price squeeze test?

Generally, margin squeeze tests should be geared to an efficient competitor, because

- only competitors run the risk of a margin squeeze
- the wording of section 28 and the preamble of the German Telecommunications Act indicate this
- more juridical considerations are supported by economic reasoning because the objective is the protection of competition
 - to achieve this, there must be the option of taking account of divergencies from the incumbent's costs



What is meant by the term “efficient competitor”?

- The term “efficient competitor” cannot be confined to a specific business model because of the market neutrality requirement
- Abstract assessment of efficient behaviour is needed to ensure efficiency within the chosen business model
- Efficient competitors in total - based upon various access services – allow competition on a nationwide basis
- For margin squeeze tests, the relevant market coverage of an efficient competitor depends on market-specific conditions



Specific cost situation of an efficient competitor (I)

- The perspective of an efficient competitor implies a number of differences compared to the incumbent's costing
 - competitor-specific costs (e.g. collocation costs)
 - the realization of fewer economies of scale and scope
 - disadvantages in terms of learning curve effects
 - higher risks due to the lack of a historically grown customer base and reputation
 - differences in customer structure that may affect usage profiles and contract duration



Specific cost and profit situation of an efficient competitor (II)

- It can be assumed that the cost differences are mainly a transitional issue, the importance of which will be substantially reduced over time
- The reputation, customer base and customer structure of former monopoly undertakings and their competitors should gradually become more similar
- Generally, we can assume that specific competitor costs such as lower economies of scale and scope, collocation costs and any differences in customer structure have (in the long run) to be compensated for in another way



How to determine the costs of an efficient competitor?

- Since the prices charged by new providers largely depend on the end-user tariffs of the dominant company there is uncertainty about the relationship between prices and their underlying costs
- For this reason, it is extremely difficult to draw sound conclusions from a comparison with competitor offers in the same market, as far as covering costs and margin squeezes are concerned
- For margin squeeze tests, the costs of an efficient competitor should be determined; as far as possible, this should be done on the basis of (approved) rates for wholesale services



Should price squeeze tests be performed per service or per basket of services?

- Whether margin squeeze tests should be restricted to individual markets or applied to rates across various markets cannot be answered in general. Consideration of the competitive conditions is required on a case by case basis.
- Since the central issue is the replicability of specific rates, the reference point depends on the business models of efficient competitors
- We allow an opening for combined rates if
 - the practicability of a margin squeeze test is not called into question
 - the bundles to be taken as a reference can also be offered by all efficient competitors in that particular combination



Thank you for your attention!

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