Country Submission for the Competition Committee Meeting 29-30 June 2011

Topic: "IMPACT EVALUATION ON COMPETITION CASE"

Introduction

The measurement of the impacts of a decision is a critical matter for an antitrust agency in measuring the extent of the effectiveness of such agency in giving benefit to consumers or the public welfare. The existence of quantitative or measurable impacts of a decision will be beneficial for internal and external dimensions. Internally, evaluation of such impacts can serves as a reference for agencies in reviewing the effectiveness of the law enforcement function of the agency. Externally, the results of such evaluation can be useful for the advocacy efforts of the agency to increase the public awareness and acceptance about the importance of the implementation of business competition law and policy. This quantitative evaluation can also become an important addition to the achievement indicators of other agencies, specifically the statistical data on the achievements in law enforcement.

Merger cases can be considered to be relatively different from other violations due to the element of remedies contained in the decision or recommendation of the antitrust agency on its in-depth analysis performed upon the merger proposals from business actors. The remedy frequently recommended is the divestment of a portion of company's assets or only allowing a merger of certain units of the merger parties. Therefore, the measurement of the impacts can be different from the evaluation of a regular case.

Analysis of impacts of a merger decision has never been conducted in Indonesia

The practice is a quite different in Indonesia. The laws and regulations on merger, in relation to the enforcement of the business competition law, have not included the element of legal remedies as an output of the antitrust agency on merger which must be notified. With the implementation of the post notification mechanism, the opinion made by the Commission for the Supervision of Business Competition (KPPU) on a merger case is limited only to the statement on whether or not there is alleged monopolistic practice and unfair business competition resulting from a merger, except upon a voluntary consultation carried out by the merger parties prior to the implementation of the merger. Upon the consultation, the commission is able to provide a recommendation for improvement, such as remedies, however without any obligation to implement the recommendation. The recommendation provided also cannot impede the authority of the commission to evaluate such merger once the merger has been conducted. As from the implementation of Government Regulation No. 57/2010 concerning merger in July, 2010, to date, it is recorded that there have been 11 (eleven) mergers notified and 2 (two) consultations. However, there is no merger affecting business competition.

In such condition, the commission has never evaluated the impact of a merger decision. However, since a merger is treated equal as other provisions, then an impact assessment of other type of competition cases would be interesting to be shared.

Currently, an in-depth quantitative evaluation has been conducted by the commission on the impacts of the commission's decision related to the case of short text message (SMS) rate cartel by several telephone operators in Indonesia, which was pronounced on June 16, 2008. It is stated in the decision that six telephone operators in Indonesia were proven to have been involved in a cartel of SMS rates causing losses to consumers

amounting up to Rp2.827 trillion (USD 332.6 million¹). Such amount was calculated based on the difference between the revenues based on the cartel price and the revenues based on the competitive price of off-net SMS. The impacts of the decision were evaluated in 2010 by the KPPU in cooperation with University of Indonesia. This written submission will explain issues and results related to this evaluation.

Methodologies

The study on the impacts of the Commission's decision on the case of SMS rate cartel was intended to measure the effects of KPPU's decision on SMS rates and the impact of an increased competition on consumer welfare. KPPU indicates 3 (three) types of measurement which are frequently used to evaluate the implication of amendments to policies on welfare, namely consumer surplus, compensating variation and equivalent variation.

The measurement of consumer welfare by using consumer surplus is derived from the Marshallian Demand Function, which indicates the quantity of demand as a function of price by maintaining a constant income in line with the change in the consumers' utility level.

Compensating variation (CV) is defined as the amount of income that must be taken away from a consumer (positive or negative) after an economic change to restore the consumer to the original welfare level. The CV is the income adjustment required to make the consumer indifferent between consuming the original basket and facing the lower price basket in different utility level.

In contrasts to the CV, the equivalent variation (EV) is defined as the amount of income that must be given to consumer (positive of negative) in lieu of an economic change to make him as well of as with the change. EV uses the level of utility after price and income changes as a basis.

Comparison of Three Methods to Calculate Consumer Welfare

	Consumer Surplus	Compensating Variation	Equivalent Variation
Demand	Marshallian Demand Function, q(p,m)	Hicksian Demand Function, q(p,u)	Hicksian Demand Function, q(p,u)
Path Dependency issue	Arise	Do not arise	Do not arise
Consumer Welfare	(P1*Q1) – (P2*Q2) in MDF	(P1*Q1) – (P2*Q2) in HDF	(P1*Q1) – (P2*Q2) in HDF

Based on the aforementioned three methodologies, there are strengths and weaknesses in each methodology and model used in the analysis to see the increase in consumer welfare due to the increase in competition where the Compensating Variation and Equivalent Variation Method do not have any path dependency issues as described in the consumer welfare method but required careful consideration in choosing between the two methods. From theoretical point of view, CV uses the new price as the base while EV uses initial price. If the study is conducted before an expected price change, EV is better suited. When the research of welfare measure has been done after a price change then CV is better suited. As for the demand function, each model usually follows certain unique econometrics method. In choosing an appropriate method, many things need to be considered especially for availability of the data that has always been a classic issue

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 $^{^{1}}$ USD1 = Rp 8,500

in developing country such as Indonesia. This study suggests the use of panel data in order to pool all the data to achieve better result.

Based on such matter and from several measurement of welfare change, KPPU and the University of Indonesia decided to employ a Compensating Variation (CV) method. In essence, CV is the compensating payment (in monetary measures) that leaves the consumer as well off as before an economic change. The economic change phenomena could be in the case of a price rise, a price decline or an income change that leads to a change in consumer's utility. The compensating payment will have positive sign if a welfare loss occurs and negative sign for a welfare gain. In this case, the verdict of KPPU is expected to create welfare gain for consumer due to its rate cut impact.

How do we design the impact?

During its establishment, it was the first time KPPU conducted an analysis of the impact of a decision of competition case (non-merger). The analysis was conducted incidentally and has not been conducted regularly. The intention to conduct such evaluation was based on the Commission's needs for authentic (quantitative) evidence of the impact of the Commission's decision on public welfare. It was intended as a supporting media for the advocacy conducted by the Commission to date.

Such study can also provide the results of data analysis in the telecommunication sector related to the structure, behavior and performance of the relevant sector. The study can also become an input for KPPU in performing law enforcement and advocacy to the government in formulating the policies on the telecommunication sector. Moreover, the results of such study are expected to be able to harmonize the policies in such sector. Furthermore, through such study, it is expected that the models and methods applied can become guidelines and references for KPPU to be implemented in other cases and conditions.

The main constraints in the implementation of this study were the availability of data and funds. The availability of data has been a classic problem in Indonesia since the government's data has not been integrated. The government's data are sometimes different from the data of business actors or associations. The government's data oftentimes relies only on the reports submitted by business actors without any clarification process. The decision on SMS cartel was chosen upon the consideration that the data available in the telecommunication industry is relatively complete in Indonesia. The next problem was the availability of funds. The lack of reliable secondary data led to the increased needs for primary data. Primary data is certainly identical to the high costs of surveys and data purchase. For those reasons, KPPU has not been able to conduct regular evaluation of the impacts of its decisions.

Evaluation of the impacts of decision should be conducted regularly, but by carefully choosing the types of cases and by focusing on the cases related to the interests of the general public. The evaluation of the impacts of decisions should also be conducted by a third party (e.g. an independent consultant or university) in order to constantly maintain the objectivity of the results of such evaluation. Currently, KPPU has had a special unit (under the Research Bureau) which is assigned to analyze the impacts of the commission's decision. This unit is relatively new so that it still has limited human resources (3 staff) and very limited funds. The duty related to the evaluation of the impacts of decisions is also still limited to maintaining coordination with third parties in designing the evaluation design and providing inputs in each stage of evaluation.

How do we conduct the study?

The arrangement of SMS rates by operators had been under the KPPU's attention for a long time since it can reduce the consumer welfare significantly. Based on the findings

and facts found by KPPU during the period of 2004-2007, there had been a price agreement among operators. Such effort is usually coordinated by the dominant player and followed by other telecommunication operators. Upon perusing the KPPU's decision, consumers obtained SMS rate cut amounting to 50-70%. Prior to the pronouncement of the decision, the rate charged to consumers was Rp350.00 per SMS, then after the decision, it decreased to Rp100.00 per SMS.

In order to find and prove alleged impacts of the decrease of SMS rates to the consumer welfare, in 2010 KPPU appointed the University of Indonesia to conduct the research. In the process, KPPU staffs were directly involved in the formulation of the term of reference for the evaluation and were directly involved in supervising the implementation of the evaluation, especially in providing inputs for the questionnaires, choice of model, the parties to be surveyed, data support and evaluation of the report delivered.

The data used in this research resulted from secondary and primary data. The primary data processed in this study was obtained from the results of questionnaires as well as interviews with respondents, while the secondary data on the telecommunication industry was obtained from several sources, namely KPPU's data on decisions and studies, telecommunication operators (in the form of annual reports), the Directorate General of Postal and Telecommunication Services (in the form of data on the number of costumers), the Central Bureau of Statistics (in the form of consumption price indices for communication and real per capita Gross Domestic Product) as well as data obtained from the internet.

The data obtained from those public sources was considered not satisfactory, such as the lack of data series before 2004 and complete data of rates so that the researcher had to determine a simple form of analysis model to ensure that the study would produce useful results. The researcher and KPPU did not have any power to "force" business actors to provide non-public information, but basically business actors were cooperative in providing the data needed since they believed that this study was quite useful and there was no internal party from the business competition agency which objected to this study.

What we have learned from this evaluation?

The research show that the KPPU's decision resulted in increased competition and significant reduction of SMS rates. By using *compensating variation* (CV) calculation method, the total consumer welfare reached approximately Rp1.9 trillion (USD 223.5 million) for the entire 6 (six) operators from 2007 up to 2009. Therefore, it can be concluded that the KPPU's decision had an important role in the increase of competition among operators and the realization of the higher total consumer welfare. The results of the evaluation also show that the KPPU's decision had an important role in maintaining competition among operators. The emergence of new players in the industry tended to encourage the reduction of rates and create competition among operators.

The interpretation of the results and the delivery of recommendations were fully conducted by the third party in order to ensure the objective results and recommendations. KPPU did not convey any objection to the conclusions or recommendations conveyed in relation to the results of the research. In fact, KPPU paid due observance of the recommendations which can be applied in the law enforcement process in the Commission.

The results of this research were subsequently published to external and internal stakeholders of KPPU through a public seminar attended by wide-ranging stakeholders, especially from business actors, academicians, governments, the press, etc. Most of the participants welcomed the results and there were a few debates in the context of the model and sample used. Public assessment was more focused on the reliability of data

and the geographically narrow samples (limited to the State's capital city). The results of this research were also disseminated through the official website of the Commission and used as consideration for the development of further evaluation.

This first research shows to KPPU that it is necessary to conduct evaluation of decision's impact in order to convince the agency and the public about the benefits of the enforcement of the competition law in Indonesia. In formulating further researches, KPPU considers it necessary to use larger amount of samples in order to obtain better results. Especially for national level surveys, *discrete choice* model can be applied for calculating the welfare effect. However, in order to actualize such matter, cooperation among relevant institutions is required, especially with the central statistics agency and Regional Governments. Online-based surveys can also be considered to be applied since it is more efficient even though it still requires further study on the appropriateness of its application in Indonesia.

Conclusions

Evaluation of the impacts of KPPU's decision on M&A has never been conducted since there has not been any rejection to date to the proposed merger. The M&A case has been treated as a general case of business competition, such as cartel, monopoly and abuse of dominant position. Therefore, evaluation of the impacts of a certain decision will be equal to evaluation of the impacts of decision related to M&A in Indonesia.

Currently, KPPU has conducted evaluation of the impacts of decision only once, namely the evaluation of the case of SMS cartel in the telecommunication sector in Indonesia. Such study was conducted by KPPU by appointing a university. KPPU was involved in the provision of the initial framework as well as inputs at every steps of research, from the choice of model, formulation of questionnaire, data presentation, recommendation of data sources, to the evaluation of the draft report.

The study of impacts was conducted by using the *compensating variation* model after the change of price behavior in the industry. Based on such model, the results indicated that the KPPU's decision was proven to have increased the competition in the communication sector and contributed to the significant reduction of the SMS rates which is useful for the community.

The obstacles encountered in conducting this research were mostly related to the availability of human resources and funds. Such problems occurred due to the fact that secondary data in Indonesia was unreliable leading to the increase in the needs for primary data. The unavailability of funds also forced KPPU to limit the samples which were only limited to the state's capital city and such study has never been conducted nationally.

This report is prepared by the Foreign Cooperation Division with valuable inputs from internal sources to contribute for series of the OECD Competition Committee Meeting in June 2011. Further information or clarification on stipulated issues may be obtained from Mr. Deswin Nur (Head of Foreign Cooperation Division) through his e-mail addresses, deswin@kppu.go.id or from our international team at international@kppu.go.id.