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# Competition Problems in Distribution Networks: The Turkish Competition Authority Involved with a Heavy Hand

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### Introduction

Electricity is an indispensable product for end-users and the electricity market has a sophisticated market structure. In the past, the generation, transmission, distribution, and retail operations of electricity were all done on public property, in a vertically integrated structure. Turkish electricity market had gone through a difficult liberalization process towards a competitive market. This process, which picked up speed in 2001 with the entry into force of the Electricity Market Law No. 4628,[\[1\]](#) moved to another stage with the Electricity Market Law No. 6446,[\[2\]](#) which came into force in 2013.

To enable access into the electricity market and to create a sector in which competition is ensured, the monopoly structure needed to be divided (Ertuna, 2010, p. 44). Dividing the monopoly structure means that transmission and distribution should be separated from generation, wholesale, and retail. After the liberalization process, while generation, wholesale, and retail electricity markets are converted to a competitive structure, transmission and distribution remained in a monopoly structure. This method of separation aimed to curb the power stemming from vertical integration.

In January 2015, to help to achieve the goal of a competitive market design, the Turkish Competition Authority (“TCA”) published a sector inquiry into the wholesale and retail electricity markets. The aim of the inquiry was to make contributions to policymakers on important subjects in the liberalization process, to provide guidance to undertakings operating in the sector, and to lay the groundwork for the creation of an efficient competition policy specific to the electricity market. The inquiry had dealt with the subjects of market power, market monitoring, transparency, and vertical integration for the wholesale markets, and the position of incumbent distribution and supply companies in the liberalization process, ensuring consumer awareness and final consumer pricing for the retail markets.

In December 2018, the TCA announced the initiation of a second sector inquiry concerning wholesale and retail electricity markets, after the developments on liberalization and reorganization of Turkish electricity market. The TCA aims to closely examine current market structure and operation, making assessments from competitive perspective in accordance with the market participants’ experiences and providing recommendations for the future. However, the TCA’s findings have not been published yet.

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When the inelastic demand for electricity and difficulty in electricity storage are taken into consideration, market power is an important source of competition problems in an electricity market (Sağlam, 2012, p. 67). Transparency has been considered as an element for preserving efficient competition in the electricity market since electricity distribution companies' subsidiaries (that is, incumbent retail electricity sales companies) and independent electricity sales companies compete with each other. Thus, determination of market power and competitive concerns that arise from market power are often on the agenda of competition authorities.

Indeed, the TCA adopted three decisions regarding the incumbent companies providing electricity distribution and retail sale services in various regions of Turkey. With these decisions, the TCA had heavily fined the investigated undertakings.<sup>[3]</sup> In this article, we will firstly examine market definition in the Turkish electricity distribution and retail electricity sales markets, and then analyze abusive practices in light of the TCA's enforcement.

### **Relevant Market Definition in Electricity Distribution and Retail Electricity Sales**

Market definition is a tool for identifying the competitive constraints that a company faces and, thus, determining who a company's competitors are. Therefore, market definition must reflect commercial realities and identify the full set of competing services. The legal standard for market definition is set within the Guidelines on the Definition of Relevant Market.<sup>[4]</sup> Principally, the TCA takes demand substitution into consideration while defining the relevant markets. Supply substitution may also be taken into consideration where its effect is equivalent to that of demand substitution.

The relevant market is established by the combination of the product and geographic markets. The relevant product market comprises all the products and/or services that are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices, and their intended use. The relevant geographic market comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and can be distinguished from neighboring areas because the conditions of competition are appreciably different in those areas.

In the electricity sector, distinctions are made among generation and wholesale services, transmission services, distribution services, and retail services during relevant market analysis. However, this article focuses on distribution and retail services, given that the TCA's enforcement relates to these markets.

Before delving into details, the current competitive framework of Turkish electricity sector should be indicated briefly. In the retail level of electricity sector, ineligible consumers may only be served by the retail arm of the electricity distribution company operating in the region where the customers reside and retail prices for ineligible consumers are determined by the Energy Markets Regulatory Authority ("EMRA"). Instead, incumbent retail electricity sales companies and independent electricity sales companies compete on equal grounds for signing agreements with eligible

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customers. This competitive framework has blurred the lines between distribution and retail electricity markets in terms of competition (Yücel, 2012, p. 7).

However, the relevant market definition for unregulated activities differs from regulated activities. With respect to distribution, the TCA defined the relevant product markets as the regional electricity distribution services markets in line with the fact that each distribution company operated as a legal monopoly in their respective regions.

On the other hand, the TCA held that the differences among residential customers, commercial customers, and industrial customers would justify defining three separate product markets for the retail sales of electricity. Thus, “*retail electricity sales to consumers under eligible consumer limits*”, “*retail electricity sales to industrial consumers*”, “*retail electricity sales to business consumers*” and “*retail electricity sales to residential consumers*” are defined separately as relevant markets. The market for retail electricity sales to industrial customers was further sub-segmented as “*retail electricity sales to industrial customers tied to the system at the transmission level*” and “*retail electricity sales to industrial customers tied to the system at the distribution level*”.

The TCA considered the difference in the regulated tariffs for each customer type, different legal rules governing the agreements to be signed with the residential customers and different awareness levels, and perceptions of the relevant consumer groups. Although the TCA had sub-segmented the relevant market, the investigated undertakings had claimed for relevant market definition based on consumption levels for commercial and industrial consumers.

Moving forward to the relevant geographic markets, it is crucial to determine whether to define a nation-wide market or a regional market. In its decisions, the TCA considered that, regardless of the type of the customer, the conditions of competition in each distribution region were considerably different from one another, as incumbent retail electricity sales companies had much higher market shares, both in terms of electricity sold and number of customers served than the independent electricity sales companies in their respective distribution regions. Although the investigated undertakings argued that the relevant geographical market should be defined nation-wide, the TCA rejected this argument and defined local geographical markets for retail electricity sales made to residential, commercial, and industrial customers.

This narrow market definition considerably affected the TCA’s assessments since the investigations concerned abuse of dominance. With respect to dominance in local retail electricity sales markets, the TCA pointed out that the market shares of all incumbent retail electricity sales companies in their respective distribution regions were much higher than their closest competitor and emphasized that the currently held market power does not seem transitory due to the presence of high entry barriers and a lack of buyer power.

### **Abusive Practices in Electricity Distribution and Retail Electricity Sales**

The dual role of the incumbent retail electricity sales companies has caused competitive concerns in

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electricity markets (Özercan, 2007, p. 26). Vertical integration creating incentives for cross-subsidization between network activities and unregulated activities, and discriminatory use of the network and access to information, are commonly considered as a source of abusive practices in the electricity markets.

The TCA brought up two main issues with respect to the creation and maintenance of a competitive retail electricity sales market. These were potential competitive advantages that may stem from the vertical integration between incumbent retail electricity sales companies and distribution companies, and incumbent retail electricity sales companies' potential incentives to leverage their legal monopoly in the market for the retail sales of electricity to ineligible customers, as well as their dominance in the competitive section of the market to distort the competition and hinder the activities of the competitors in the unregulated market.

In 2014, the TCA had conducted preliminary inquiries against certain distribution companies and incumbent retail electricity sales companies to assess whether they had abused their dominant position.<sup>[5]</sup> Although the TCA identified certain unilateral practices of the vertically integrated undertakings that may have restricted competition in various regional markets for retail sale of electricity, instead of initiating fully fledged investigations, the TCA addressed structural problems in the market to the EMRA. Moreover, the TCA sent warning letters to the companies requiring the cessation of the examined practices.

Almost four years later, the TCA had initiated fully fledged investigations against the vertically integrated undertakings in Turkish electricity market. The TCA examined allegations of:

- Anticompetitive information exchange and coordination between the distribution company and the incumbent retail electricity sales companies
- Foreclosure of the market to the independent electricity sales companies through different conducts
- Complication of customer switches to competing independent electricity sales companies via concluding legally deficient contracts and IA-02 Forms
- Competition in the market being restricted due to the implementation of different conducts
- Customer switches being prevented via agreements including commitments and automatic renewal clauses.

As a consequence of the extensive investigations, the TCA decided that the investigated undertakings violated Article 6 of the Law No. 4054 on the Protection of Competition.<sup>[6]</sup> Although the infringement findings for each investigation slightly differs from each other, the TCA has identified discriminatory abusive practices in the electricity market.

It was concluded that this vertically integrated undertakings violated competition by disadvantaging other independent retail electricity sales companies. The TCA ruled that the investigated undertakings foreclosed relevant markets by means of eliminating eligible consumer mobilization process and breaking down the consumer choice mechanism, and thus abused its dominant position

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in the relevant market.

## **Concluding Remarks**

The TCA's decisions reveal that it assigns significant value to the electricity markets. The alleged narrow market definition made by the TCA has put incumbent retail electricity sales companies in a difficult position. By reason of the narrow market definition, the incumbent retail electricity sales companies held a dominant position in their respective distribution regions. Thus, their commercial strategies should be determined carefully considering the special responsibility that arises from the dominant position. The TCA's vigilant approach to electricity markets shows that the TCA will not hesitate to use its enforcement powers against the incumbent undertakings, and the TCA's ongoing sector inquiry may shape the competitive structure in the electricity market.

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[1] Published in the Official Gazette No. 24335 (Repeated) and dated 3 March 2001.

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[2] Published in the Official Gazette No. 28603 and dated 14 March 2013.

[3] The TCA's decisions dated 20 February 2018 and numbered 18-06/101-52; dated 8 August 2018 and numbered 18-27/461-224; dated 1 October 2018 and numbered 18-36/583-284.

[4] Adopted by the TCA's decision dated 10 January 2008 and numbered 08-04/56-M.

[5] The TCA's decisions dated 22 October 2014 and 14-42/762-338; dated 22 October 2014 and numbered 14-42/761-337; dated 3 December 2014 and numbered 14-47/860-390.

[6] Published in the Official Gazette No. 22140 and dated 13 December 1994.