

Kluwer Competition Law Blog

Market Design in Household Waste Collection in Ireland: Competition in or for the Market?

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Introduction

The collection of household waste (HHW) in Ireland is currently a private sector activity. Individual households contract with private operators for the provision of the service. Subject to fulfilling certain regulatory requirements any private operator can enter the HHW collection market and by offering better terms and conditions – competing on the merits – persuade households to switch their HHW provider from an existing operator (i.e. side-by-side or competition *in* the competition). The street I live on in Dublin City, for example, is currently serviced by two HHW collectors, down from three a year or so ago. But is this the optimal market design for HHW collection? Are there better alternatives? What does the evidence suggest?

The Competition and Consumer Protection Commission HHW Study

A review of household waste policy in Ireland is to be initiated in 2019. An important input into that review is the Competition and Consumer Protection Commission (CCPC)'s September 2018 study (the study) on the operation of the HHW market. The study found that in part due to economies of scale and density that the HHW collection market was evolving into a series of monopoly providers, "*which will ... increase their charges.*" Over the period 2012 to 2016 the number of HHW operators declined from 82 to 63, a reduction of almost a quarter. So much for the market failure; what about the solution?

The CCPC called for a national economic regulator that would issue economic licenses for HHW operators, conduct research, levy fines and, crucially, determine the appropriate market design for each geographic market it identified: the existing side-by-side model; competitive tendering (i.e. competition *for* the market); and/or price control. The CCPC did not express a view on the optimal market design for HHW collection.

Counterintuitive?

To an outside observer the recommendations of the CCPC seem to be counterintuitive. In many

jurisdictions the market design for HHW collection is via a monopoly provider selected through competitive tendering. There are good reasons for such a choice. HHW charges are lower than side-by-side competition since not only are economies of scale and density realised but monopoly rents are eliminated. In 2012 a careful comparison of HHW charges between Cork (side-by-side competition) and Belfast (competitive tendering) found that annual HHW charges were 30 per cent lower in Belfast.

CO₂ emissions and congestion costs will be reduced under competitive tendering as there will be no inefficient duplication of services. Mechanisms can be introduced that complement competitive tendering so as to ensure that HHW collection charges do not get too high in low density areas, thereby protecting positive externalities of broader take-up of HHW collection services.

Furthermore, since the CCPC sees the HHW “*market ... moving towards a service provision of unregulated monopoly operators,*” this would at first glance appear to favour competitive tendering as the preferred market design.

A National HHW Economic Regulator: Ex Ante Regulation

In deciding the appropriate market design the CCPC applies a threefold test to the side-by-side model. The three fold test is drawn from that applied by the European Commission to determine whether or not ex ante regulation is justified in the case of telecommunication markets. The tests are cumulative. All three tests have to be satisfied in order to merit the introduction of ex ante regulation. Ex post is the default. In order to justify ex ante regulation a market must exhibit: high barriers to entry; lack of effective competition; and, insufficiency of competition law. The CCPC successfully demonstrates that these three conditions are satisfied in the case of side-by-side competition.

Competitive Tendering: Ex Post Regulation

This raises the question of whether the three criteria would be satisfied if the market design were competitive tendering.

The first criterion to justify *ex ante* regulation is the “*presence of high and non-transitory barriers to entry,*” is not attained under competitive tendering. Barriers to entry are low to medium as compared to the high barriers to entry under side-by-side competition. But on what basis can such a conclusion be reached when the same non-transitory economies of scale and density are present? The answer revolves around the nature of competition. Under side-by-side competition incumbents may have scope to reach tacit agreements and understandings not to compete with rivals in adjacent geographic markets, while the ability to cut prices selectively combined with economies of scale and density (i.e. low if not zero marginal costs) discourages new entrants.

Under competitive tendering, competition takes place for the right or the contract to supply the HHW collection service as specified in the tender documents. The incumbent has few if any advantages over new entrants, provided that enough reliable market information is provided to bidders. Reaching tacit understandings as to which collectors would win particular tenders would be difficult to enforce in view of the strong incentives to cheat with tenders awarded for substantial periods of time, typically five to seven years.

The second criterion to support *ex ante* regulation is that “*market structure ... does not tend towards effective competition within the relevant time horizon.*” The evidence suggests that this condition is not met. There are three (and maybe more) classes of bidders: collectors that currently serve a series of geographic markets in Ireland; others with a more local or regional focus; and, international bidders which have been reportedly discouraged from entering the Irish market due to its side-by-side nature (i.e. the costs, difficulties and uncertainties of ensuring enough existing households switch so as to make entry profitable). Incumbent HHW operators are likely to have developed expertise in competitive bidding or tendering in various commercial waste streams, while international bidders would often also be familiar with HHW tendering. The use of common tenders and standard documentation lowers the costs of bidding and hence is likely to encourage more rather than fewer bidders.

The third criterion is that the “*insufficiency of competition law alone to adequately address the market failure(s) concerned.*” Again the criterion is not met. There are a number of ways in which firms can thwart the impact of competitive tendering and thus lead to market failure. The most obvious is for potential bidders to allocate bids by local authority area so that prices will exceed costs, where costs include a normal rate of return. In other words, rents would be earned.

As noted above, the diversity of firms bidding for the HHW contracts and the strong incentives to cheat make successful bid-rigging problematic. However, notwithstanding that, such bid-rigging is subject to a by object prohibition under the Competition Act 2002. Hence collectors run the risk of criminal prosecution resulting in fines and/or jail sentences. Potential bidders should be made aware of these consequences and advice should also be sought from the CCPC as to the optimal timing of procurement competitions so as to minimise the opportunity for successful bid-rigging.

In relation to merger control there is always the danger that especially aggressive bidders could be acquired by incumbents to prevent such mavericks from disrupting any tacit or formal market place agreements. The Competition Act 2002 prohibits mergers that substantially lessen competition. The difficulty here, as identified by the CCPC, is that many HHW mergers are below the mandatory turnover notification thresholds. However, there are provisions within Ireland’s competition law to specify classes of mergers that have to be notified to the CCPC irrespective of the turnover.

Conclusion

In sum, given the environmental and price advantages of competitive tendering as compared to side-by-side competition, the application of the three fold test, the evolution of the HHW market in Ireland towards a series of monopoly providers, and the CCPC study’s observation that “*regulation ... is only undertaken as a last resort due to actual or expected market failure,*” strongly suggests that the 2019 review of household waste policy in Ireland should recommend the introduction of competitive tendering as the preferred market design. Tendering could be administered through local authorities. This is the practice elsewhere, while in Ireland when the public sector directly provided the service it was through local authorities. The local authorities could be assisted in the timing, design and monitoring of tenders by the CCPC and the Office for Government Procurement.

This blog is based on a Munich Personal RePEc Archive Paper: <https://mpra.ub.uni-muenchen.de/95000/>. The research for this blog was conducted while the author was a visitor at Concordia University, Montreal. I should like to thank Ian Irvine for inviting me. The author was a member of the Competition Authority between 2000 and 2008 responsible for the Authority's 2005 enforcement decision on household waste collection. Subsequently he advised the agency on the issue of market definition in M/16/008 – PandaGreen/Greenstar. Apart from a meeting on 25 October 2017 with the CCPC to discuss the terms of reference for its HHW study, the author had no involvement in the study. I am grateful for comments by Ian Irvine, Sean Lyons and Francis O'Toole. The usual disclaimer applies.

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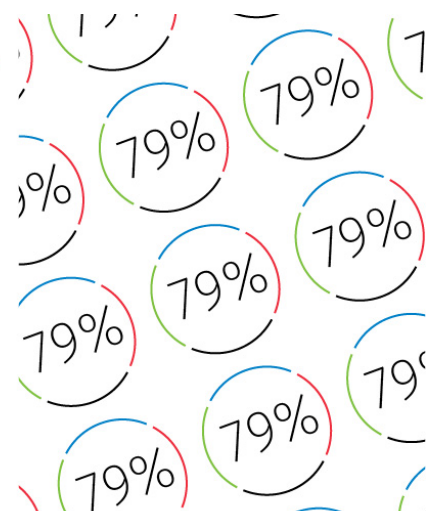
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