

## SSNIP Test: A Useful Tool, Not A Panacea

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*The origins of the modern competition law are, generally, traced to the enactment of Sherman Act in 1890 in USA. Moving on to its onward journey, the competition law, known as Anti Trust Law in USA, evolved over a period of time. In this journey, reliance slowly tilted more towards the “effects” or “rule of reason” approach in contrast to the “per-se” approach. As a means to define the relevant market for assessing the impact on competition, of any merger, the concept of Small but Significant Non-transitory Increase in Price (SSNIP) test was expressed, for the first time, in 1959. This idea of SSNIP test as a tool in determining the relevant market was also included in the US Merger Guidelines of 1982 indicating popularity of its use. Over a period of time, it has gained considerable acceptance in determining relevant market. However, the enhanced popularity should caution us into over dependence on this wonderful tool. So much so that, sometimes, a view is held that without conducting a SSNIP test a relevant market cannot be defined. We should not forget that prior to 1959 also, the competitive assessment of various mergers, was being done. Instead of following a particular method, the determination of the relevant market was being done intuitively. Aim and objective of any competitive assessment is to see the adverse effect on competition. Anything which aids and assists in this assessment is only a tool. This article high lights this basic fact and urges that SSNIP test should be used as a good tool with all its limitations kept in mind.*

### 1. Historical Background

A market is defined as a product or group of products and a geographic area in which it is produced or sold such that a hypothetical profit-maximising firm, not subject to price regulation, that was the only present

and future producer or seller of those products in that area likely would impose at least a “small but significant and non-transitory increase in price,” assuming the terms of sale of all other products are held constant.<sup>1</sup>

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<sup>1</sup> US Horizontal Merger Guidelines, 1992, issued jointly by the Department of Justice and the Federal Trade Commission.

The above reference to SSNIP is considered to be the official recognition to SSNIP test. The concept was not new at the time. It was included in the 1982 US merger guidelines and Adelman expressed the core idea in 1959.<sup>2</sup>

The Small but Significant and Non-transitory Increase in Price (SSNIP) is taken to be either 5 per cent or 10 per cent. Therefore, it is also known, sometimes, as 5-10 per cent test. The guiding principle of Hypothetical Monopolist (HM) test is "a relevant market is something worth monopolising".<sup>3</sup> This HM test is increasingly being adopted by competition authorities through out the world. Some of the jurisdictions using it in one form or the other, are:

Australia, Brazil, Bulgaria, Canada, EU, Israel, Netherlands, New Zealand, UK, USA.<sup>4</sup>

## 2. The Test

The SSNIP test is a tool in product market definition in which a minimal possible sub-set of products is taken for analysis of finding out relevant product market. It is seen if a theoretical HM, if having an option, will increase the prices of the products in a non-transitory way. Or is it possible that even if the HM, producing those goods, which fall in the subset referred to above, raises the prices, the market forces would ensure that prices do not remain remunerative for this HM. This can be on account of a number of factors. Either the consumers may start sourcing the products from alternate sources, or on account of availability of other substitutable goods, it will not be remunerative, in the long run, to keep on manufacturing the concerned products in the market.

This may be on account of the fact that the ease of entry into and exit from the market are such that, it does not take very long for the producers of substitutable goods to enter the market and start producing the same goods and making them available at competitive prices to the consumers. Thus, the possibility of a HM raising price in a small but significant manner is only possible if these type of constraints, on anti-competitive forces, in the present status of equilibrium, do not exist. If such alternative sources exist, the HM will have a restraint against increase in price in small but significant manner in and non-transitory manner.

After having started from the product, in question, and an extremely close and unambiguous substitute products in the relevant product market, a question is asked if a HM is producing those products, would he be in a position to effect a SSNIP.

In other words, this is relating to the transferability of demand or degree of transferability within closely related products amongst which substitutability exists. This could also be understood as that domain of products which, if comes within the control of the HM, would encourage him to effect a SSNIP. If HM is supposed to be a monopolist, he would not affect a SSNIP unless he is certain that the gains accruing to him from the persons leaving his custom are more than made up by the extra revenues bought in by the price increase affected by him. If he knows that the gains by SSNIP are more than offset by the consumers leaving his offer, it would be foolish to affect such a SSNIP.

<sup>2</sup> Morris A. Adelman, *Economic Aspects of the Bethlehem Opinion*, 45 VA. L. REV.684, 688 (1959).

<sup>3</sup> Bishop and Darcey (1995)

<sup>4</sup> Bishop and Walker (2002), *Sweet and Maxwell*, Page 88, Para 4.12

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Once a HM knows that if he is affecting a SSNIP, either all the customers would take the products offered by him or take the substitute products which would be also under his control, he is more likely to affect a SSNIP. Therefore, the HM would affect a SSNIP only if he is certain that the customers would not move out of this chosen basket of products.

This iterative procedure is repeated till we reach a product set where we are sure that the HM will affect a SSNIP if he controls this set of products. There cannot be any discrete point up to whose products are to be included in the set. This process is extended by judgment about substitutability gradually.

The European Commission has also endorsed the SSNIP test as a method for market definition by including this test in its notice for mergers in the relevant market definition.<sup>5</sup>

### **3. SSNIP Test is a Means and not an End**

This test is a means for defining relevant product market and not an end in itself. Competition Commission, UK states that SSNIP test is not an end in itself, but a framework within which to analyse the effects of a merger on competition. Competition Commission UK, normally,

uses 5 per cent for SSNIP test and not the common 5 to 10 per cent.<sup>6</sup>

### **4. Unique market Definition not Necessary**

The test also depends on the characteristics of the product. Where a judgment regarding bringing new products into the product market sub-set is concerned, it is most likely to be affected by the judgment of the person applying test. To say that it is very scientific is correct only to limited extent. In its application, human judgment does come into play. The physical characteristics of the goods, under consideration, and the perception of the personnel applying the SSNIP test will play a role and to say that a test would be absolutely scientific may not be correct.

There cannot be a mechanism by which one can draw a straightjacket to decide that so many products would be considered in the product market for SSNIP test and all others would be out. It is natural that the characteristics of the product should determine the market definition to some extent. It is for this reason that depending upon the sequence in which products are included in the relevant product market, HM test may lead to non-unique product markets.

### **5. Limitations**

If the HM is already charging monopoly profits, there is no further scope of any price rise. It would mean that the SSNIP may lead to a very wide market. This is known as "cellophane fallacy". Thus, SSNIP test fails in case of a firm already possessing market power.<sup>7</sup> This is known after the *Du Pont*<sup>8</sup> case. There, Du Pont argued that

<sup>5</sup> Commission notice on the definition of the relevant market for the purposes of Community Competition Law", Official Journals, OJ [1997] C 372 .

<sup>6</sup> OFT Market Definition Guidelines, Para 2.1.

<sup>7</sup> "The role of market definition in monopoly and dominance inquiries", Economic Discussion Paper 2, Office of Fair Trading (OFT 342)

<sup>8</sup> *U.S. v. El du Pont de Nemour and Co* 351 US 377 (1956)

cellophane was not a separate relevant market. At prevailing prices, cellophane could be shown to have a high cross-price elasticity of demand with flexible packaging materials such as aluminum foil, wax paper and polyethylene. However, these products can only be regarded as providing effective competitive constraints preventing Du Pont from increasing the price of cellophane above competitive levels if the prevailing price is the competitive price. The US Supreme Court failed to recognise that a high own-price elasticity and the identification of effective substitute of prevailing prices may merely be the result of the exercise of existing market power.<sup>9</sup>

Another mistake of focusing on the behaviour of particular groups of consumers or on average consumers, in the process of defining relevant market has been referred to as “toothless fallacy”. This follows the *United Brands*<sup>10</sup> decision in EU.

## 6. Product Characteristics

The HM test is contrary, to what many commentators have suggested, concerned with non-price elements of competition and does take account of physical characteristics and intended use.<sup>11</sup> It should be mentioned that although this test refers to only price but non-price elements such as the quality of the competing product, physical characteristics and intended use are all integral to SSNIP test.<sup>12</sup>

## 7. Whether Leads to a Bad Market Definition

This does not mean that this leads to bad market definition. At least, there is some

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yardstick to go, in a step by step manner, to determine the market. If even this process is not there, in that event, the market definition would become highly subjective. At least, there is an attempt to make the process of market definition as scientific as possible.

It would be nearly impossible to divest the SSNIP test, in reality, from dependence on empirical evidence and observations. As indicated above, in the preceding paragraphs, this is an iterative process for product market definition.

The objective of SSNIP test is to determine, in as much scientific and systematic way as possible, identify and define the boundaries of competition between firms.<sup>13</sup> The SSNIP test can be treated as a method of classification. Irrespective of the dream demarcation, in the mind of competition analyst, working as an outer boundary between the group of products within the relevant product market and the outside market, it is really not possible to find such water tight demarcation.

Characteristics of products/services do matter. All the products/services are, generally, identified by their features or service characteristics. “Zero-One” kind of demarcation may not exist.

<sup>9</sup> Bishop and Walker (2002), Para 4.36

<sup>10</sup> *United Brands Co. v. Commission* (1978) E.C.R.207: (1978) 1.C.M.I.R. 429

<sup>11</sup> Richard Whish (2005) Competition Law 2005.

<sup>12</sup> Bishop and Walker (2002), Sweet and Maxwell, Page 86 Para 4.09

<sup>13</sup> Commission notice on the definition of the relevant market for the purpose of community competition law.

This test does not give any guidance as to which product should be added to the SSNIP candidate market and in which order. The possibilities of most products/ services and their classification would depend how their characteristics are either compared or differentiated. Therefore, to say that the SSNIP test should be absolutely scientific would be incorrect. Assessment for the characteristics of the product is going to play an important role. Out of the available possibilities, this has been found to be reasonably good systematic method and has survived nearly a quarter of a century.

It is widely recognised that the evidence relied upon to define relevant markets includes items in the product dimension, depending very much on the characteristics and specificity of the industry and products or services that are being examined. If two products are physically very different to the extent that they cannot in fact be used for the same end use, they cannot be considered as substitutes.<sup>14</sup> The EC defined separate markets for trucks of 5 to 16-ton trucks in *Volvo/Scania*.<sup>15</sup> There have been cases in which commonality of physical characteristics or intended use is used to suggest the existence of effective substitutes.

In *Nestle/Perrier*,<sup>16</sup> the parties argued that, in addition to bottled water, the product market included all non-alcoholic beverages on the basis that products in this market had the same basic function of quenching the thirst of the consumer. The EC asserted that when purchasing

bottled water, the consumers were not simply seeking to quench their thirst but were seeking to do so with liquid form a healthy source. Thus, soft drinks were excluded. However, on this definition the market seemed to include purified tap-water (which meant that Coca-Cola would have been a potential entrant as all Coca Cola bottlers are required to start with purified tap-water before adding the Coca-Cola syrup and bubble). To eliminate this possibility the Commission added that consumers were seeking to quench their thirst with liquid from a healthy, natural source that provided minerals.

### 8. Conclusion – A Helpful Tool

Thus the SSNIP test is indeed a helpful tool in arriving at the definition of relevant product market. In absence of SSNIP-prior to the test being suggested around 1959 or even before it became popular- also relevant product markets were being defined. However these would, naturally, by an intuitive process. Use of SSNIP test has provided a methodology for systematically arriving at the definition of “relevant product market”. It does not mean that competition law did not exist before SSNIP emerged on the scene. It did. The only difference it made was that of adding one more tool in the tool kit of a competition law analyst. Therefore SSNIP should be accepted as it is – a helpful tool and not a “be all and end all” in competition law assessment.

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<sup>14</sup> Bishop and Walker (2002), Para 4.48

<sup>15</sup> *Volvo/Scania*, Case COMP/M.1672

<sup>16</sup> Case IV/M 190(1993) 4 C.M.L.R. M17(1992)O.J.L.1.356/1