The Commission formally rejects two complaints in the electronic monitoring services field

Miguel Ángel PEÑA CASTELLOT, Directorate-General Competition, unit C-3

1. The complaints

On 19 November 2001 (‘the first complaint’) and 1 July 2002 (‘the second complaint’) respectively, the UK-based firm On Guard Plus Ltd. (“OGPL”) filed complaints against the Israel-based firm Elmo-Tech Limited (“ELT”) for alleged violations of Article 82 of the EC Treaty.

In the complaints, OGPL held that ELT was dominant in the EEA-wide market for the provision of field hardware for the electronic monitoring of prisoners. As described below in further detail, the only piece of evidence provided by OGPL in support of its allegation of dominance was a table compiled by it showing that ELT had a 60% market share in that market.

OGPL claimed that ELT had abused its alleged dominant position, first by engaging in predatory pricing aimed at driving other market players out of the electronic monitoring systems market (the first complaint) and, second, by refusing to supply its field hardware to OGPL (the second complaint).

2. The products

Both complaints were about electronic monitoring systems (‘EMS’). These are systems that enable the non-stop monitoring of individuals by ensuring they are at a certain place during certain hours of the day. They are mainly used in the penitentiary sector where they provide an alternative for prison orders (primarily in cases of pre-trial detention and short prison sentences) and make early release possible.

EMS are composed of electronic monitoring products on the one hand, namely an electronic bracelet and an in-house monitoring unit in the offenders’ homes (together the field hardware) and a central computer (the base hardware), and electronic monitoring services on the other hand, provided by both IT and control staff and by security intervention staff.

Offenders are normally monitored at their own homes. The electronic bracelet, fitted to the ankle or wrist, emits a signal that is received by the in-house monitoring unit, which is a small device plugged into the power supply and to the telephone socket outlet. The equipment alerts the control centre about any unusual movement or tampering with either the bracelet or the monitoring unit.

The information received by the in-house monitoring unit is reported to the central computer system via the telephone line, enabling control staff to check the information on the central computer. Special software installed there allows follow-up of each particular offender, in accordance with the particularities of the relevant detention regime, and produces reports and alerts.

EMS have been in use in the US since the late 1980s. Some 90% of all offenders subject to an EMS regime are in the US. The use of such systems in Europe is still in its infancy. EMS were first tried in England in 1995, followed by Sweden shortly thereafter. Many European countries are now introducing EMS. Before deploying a large-scale national EMS programme, penitentiary authorities normally first test out EMS by setting up pilot projects. Besides England and Sweden, the Netherlands, Spain, France, Italy and Scotland have launched such pilot projects. New tenders are to be launched in Europe in the near future, in particular in continental Europe (e.g. in France or Italy), and are likely to be of a much larger size than those awarded so far.

Procurement of EMS for both pilot projects and full programmes is made through open call for tenders. In general, penitentiary authorities rent or lease the necessary products and/or services. Prices are usually expressed as an amount per day/per offender. There are nevertheless differences: whereas in the UK and in the US penitentiary authorities not only rent or lease the field and base hardware but also the control and intervention staff and services from the EMS providers, in continental Europe the monitoring services are provided by the penitentiary authorities themselves.

The contractual arrangements concerning full programmes vary between countries. Sometimes (e.g. in Sweden), the contract covers an initial small batch of firm orders for field and base hardware to be supplemented, at the discretion of the penitentiary authority, by subsequent orders of field hardware units up to a maximum number specified in the contract. In other countries (e.g.
Spain), the penitentiary authority just indicates the maximum daily price per prisoner it is willing to pay and the average number of prisoners expected to be monitored on a yearly basis for the duration of the contract. Still on other occasions (e.g. Portugal), the contract merely indicates the maximum number of prisoners expected to be monitored; a figure that would be reached when the contract approaches its termination.

Pilot projects are for the rental of a fixed number of units for the duration of the contract.

In England and Scotland the winner of a tender subcontracts the provision of the field hardware to other companies. For instance, OGPL is providing field hardware to Securicor Custodial Services in one area in England. OGPL rents the field hardware from ELT or others and then rents it to Securicor Custodial Services.

In continental Europe, e.g. in Portugal, there is sometimes a contract established between the members of the winning consortia providing for the distribution of tasks. In other cases, there is no written agreement. When preparing a response to a tender, companies willing to apply for a given tender will simply verify over the phone the availability of certain manufacturers that they normally work with.

3. The issues at stake

As OGPL brought allegations under Article 82 EC against ELT, before assessing the abusive nature of the behaviour at stake, it was necessary, first, to define the relevant markets affected and, second, to verify whether ELT was actually dominant in any of them. It will be shown below that, at the end of the day, the information at the disposal of the Commission clearly showed that such dominant position did not exist.

3.1. The relevant markets

The Commission identified two relevant markets in the present cases: a downstream market for electronic monitoring systems for the constant monitoring of prisoners, the geographic scope of which would be at least the EEA, and an upstream market for the supply of field hardware, the geographic scope of which is the EEA.

It is interesting to note that whereas OGPL is active only in the downstream market, ELT is currently active in both, although it entered the downstream market only a couple of years ago.

The downstream market for electronic monitoring systems for the constant monitoring of prisoners is clearly demand-driven. Demand for EMS comes from penitentiary authorities that want to introduce such systems as an alternative to prison sentences and that procure the EMS systems through open call for tenders.

As for the upstream market for the supply of field hardware, demand comes from Companies such as OGPL, Belgacom Alert Services (1) or Securiton (2) that do not produce field hardware and need such equipment in order to apply for tenders. The Commission confirmed that there is no ready substitutable product these companies could turn to in order to fulfil that need. As regards supply side considerations, the Commission also ascertained that entry into the market in most cases is made by companies using know-how or even existing assets for the production of field hardware and not from manufacturers of other technical equipment. In other occasions, entry was made by companies active in the same product market, but in a different geographic market (i.e., the US).

3.2. Absence of dominance

The Commission found that the distinctive features of the relevant markets together with the position of ELT therein made it impossible to conclude that ELT was dominant in any of them.

As regards the upstream market, the Commission ascertained first that a substantial number of companies are currently running pilot or full EMS programmes in the EEA. In many cases, these firms were created ad hoc to tender for and then run the relevant contracts. They did not then have any previous experience in the market.

As for ELT’s position in that market, out of the 10 full programmes currently operational in the EEA, ELT won 1 and is present in a further 2, none of them in England – where by far the most important current programmes in the EEA exist. As for pilots, ELT is running just 6 out of 14. On the basis of these facts, the Commission concluded that ELT’s market share could not possibly exceed 30% of the downstream market.

That figure is normally not indicative of dominance. Nor was the wide diversity and abundance of firms active in the market. Furthermore, the Commission looked into two very important

(1) The company to which the tender in Belgium was awarded.
(2) The company running the programme in Switzerland.
distinctive features of the market, very much linked its demand-driven nature, namely: its bidding nature and the very high degree of countervailing power enjoyed by penitentiary authorities.

In bidding markets, a high market share normally is an ex post indicator of low prices, not an ex ante indicator of high prices. What really matters in such a market is the existence of a significant number of likely bidders willing to apply for tenders. In the present cases, the reality was that many inexperienced firms were running national programmes. The Commission also had evidence that it is normal that many firms apply for a given tender (1).

The Commission also found many concrete instances of the countervailing power of penitentiary authorities being exercised.

As regards the upstream market, the Commission based its conclusion as to the absence of dominance on a number of elements.

As a preliminary issue, the Commission had many methodological concerns as regards the way OGPL had calculated the alleged 60% market share enjoyed by ELT. In particular, the Commission confirmed that the table included a significant number of field hardware units (2) either not manufactured and sold, and certainly not in use by September 2001—the cutting date for the compilation of the data included in the table— or belonging to tenders not even awarded by that date. On that basis, the ‘real’ market share of ELT as calculated by OGPL should in fact have been below 45%.

Such a figure is not sufficient in itself for a finding of dominance. On top of that, the Commission found that OGPL had significantly underestimated the real importance of actual competitors in the EEA. In fact, if the actual competitive constraints posed by such competitors were taken into account, ELT’s market share in the last two years and a half could not be significantly above 30%. By the same token, OGPL had also underestimated the real importance of potential competitors—most currently active in the US—that could enter in force in the near future once the size of tenders in the EEA grow.

It is worth noting that the Commission was able to support its assessment of the importance of competitors with a number of internal documents and e-mails of OGPL.

The same pieces of evidence clearly showed that, until recently, OGPL considered ELT as a fragile competitor the survival of which was far from granted. It is interesting to note that the market shares attributed by OGPL to ELT for the same period were largely over 90%.

Finally, even if ELT’s market share in the upstream market would have been close to the figure alleged by OGPL, competitive conditions in the downstream market were, in the opinion of the Commission, largely sufficient to exclude the existence of any dominant position that ELT could abuse in the downstream market.

The opportunities for ELT to exercise its alleged market power in a way incompatible with Article 82 EC will be limited to the relatively rare occasions when tenders are organized and severely hampered if not totally impeded by the countervailing power of penitentiary authorities.

It has to be added, that ELT (as any other manufacturer) has no control on the decisions about the organization and award of tenders. In addition, the abundance of competitors in the downstream market is clearly at odds with the type of exclusionary practices alleged by OGPL. What is more, the expected rapid growth of the downstream and, consequently, of the upstream markets in the near future in the EEA made any finding of dominance even more unlikely.

4. Conclusion

As described above, the evidence at the disposal of the Commission did not support the alleged dominance of ELT on either of the two relevant markets considered.

In the absence of a dominant position, it was, of course, not necessary to assess the allegedly abusive practices by ELT as set out in the complaints. Nor was it necessary to assess whether trade between Member States was affected.

OGPL was informed of the above analysis and conclusions by means of a formal rejection decision signed by Commissioner Monti on behalf of the Commission.

---

(1) In one national programme, 7 firms—most ad hoc consortia—replied to the tender. 3 out of the 7 were allowed to present final offers.
(2) The proxy used to measure market shares.