ANNUAL REPORT ON COMPETITION POLICY DEVELOPMENTS IN THE UNITED KINGDOM
(2006-2007)

This report is submitted by the Delegation of the United Kingdom to the Competition Committee FOR
INFORMATION at its forthcoming meeting to be held on 17-18 October 2007.
1. Executive Summary

1.1 Key Achievements

1.1.1 Investigations

1. 2006–07 was an important year in competition enforcement in the UK, with a number of key decisions in cases and in appeals before the Competition Appeal Tribunal (CAT). The OFT’s casework, which covers both investigations and the handling of appeals, was characterised by a high degree of innovation this year. That period also saw the ORR make the first infringement decision by one of the UK’s sectoral regulators with concurrent powers to enforce competition law. And the CC published reports in respect of 3 market investigations and 9 merger inquiries and developed its processes and analytical methodology.

2. The OFT continued its groundbreaking approach to seeking speedier resolution of large-scale cartel cases by offering a fast-track procedure to companies involved in our ongoing construction cartel investigation. The OFT’s two-year investigation uncovered evidence of unlawful practices in thousands of tenders with a combined estimated value approaching £3bn.

3. The OFT used its criminal enforcement powers under the Enterprise Act in two separate cases, the investigation of air passenger fuel surcharges and the on-going construction cartel.

4. The OFT resolved a competition case against 50 independent schools as a result of which a charitable trust was set up by the schools concerned to distribute settlement funds totalling £3m to the pupils affected.

5. The OFT examined a wide range of markets to assess if they were working well for consumers, and referred the markets for groceries, Payment Protection Insurance and the supply of airport services by BAA to the CC for further investigation.

6. The OFT commissioned the first independent evaluation of a completed study (new car warranties) to identify how, if at all, the market had changed as a result of our intervention, and whether the OFT could have used our powers and resources to better effect. The conclusion was that, in this particular study, consumers and fleet operators saved between £120-£170m and the cost to complete the study and follow-up activity was only £300,000.

7. The OFT piloted its use of merger simulation to measure the impact on consumers of our mergers work. The OFT estimated that consumers save around £52m a year as a result of the OFT’s mergers work alone.

8. In 2006/07 the CC completed nine mergers many of which attracted considerable public interest over the year: the merger of HMV/Waterstone’s and Ottaker’s; the Stagecoach/Scottish Citylink decision, involving a completed joint venture over two sets of long distance coach routes, aroused political and media interest when the CC was required divestment of part of the business. Six merger investigations were ongoing at the end of the period.

9. The CC reported on the domestic bulk liquefied petroleum gas, classified directors and home credit market investigation (door step lending). The findings from the latter will help some two million people who borrow small amounts of money - many of whom are on low incomes. The CC has highlighted potential savings to consumers of at least £75 million a year. Work on four additional market investigations (Personal Account Banking Services in Northern Ireland, Payment Protection Insurance and...
Airports) was ongoing at the end of the reporting period of this report. The CC also received the compulsory quinquennial reference from the Civil Aviation Authority of the London Airports price control.

10. The CC’s estimated that extra costs customers would have paid, were it not for the CC’s decisions over 2006-07 was around £322 million.

1.1.2 Appeals

11. The OFT used Article 15(3) of the Modernisation Regulation, which allows us to make written and oral submissions in cases concerning Articles 81 and 82, for the first time to intervene in the Crehan case in the House of Lords.

12. The OFT intervened in support of OFCOM successfully in the Floe Telecom case in the Court of Appeal to establish limits to the powers of the CAT to give direction to regulators.

13. In the Casting Book and Cityhook appeals, the OFT obtained confirmation from the CAT that the OFT could close a case on resource grounds without this decision being subject to a full merits appeal.

14. The OFT gained useful clarification from two appeals to the CAT – by the London Metal Exchange (LME) and MasterCard – during which our decisions were withdrawn and set aside respectively. The CAT’s costs judgment in the LME case shed particular light on the test the OFT must apply when considering applications for interim measures under the Competition Act.

15. The CC was challenged in relation to its decision to put in place interim measures at an early stage of its inquiry. The CC put in place measures to ‘hold separate and maintain measures’ in respect of the merged businesses, prevent further integration and require the separation of the management teams that already been integrated. The CC’s power to do so was upheld by the CAT. This was the second challenge of the CC’s decision under the Enterprise Act 2002.

1.1.3 Restructuring

16. The OFT embarked on a programme of radical change inside our organisation, designed to increase the benefit the OFT provides to consumers and business in the coming years. This allowed us to understand and analyse markets better, and to address problems in the way markets work using the full range of tools and methods of resolution available to us.

17. In addition, we made two significant senior board-level appointments of executive directors Jonathan May and Sean Williams, and in April 2007 we welcomed three new non-executive directors – Bronwyn Curtis, Professor Frédéric Jenny and Alan Giles.

18. This year saw a substantial refocusing of the OFT’s competition casework in line with the recommendations contained in the National Audit Office (NAO) report of November 2005 and the House of Commons Public Accounts Committee report of May 2006 (HC 841).

19. The OFT took steps to ensure that our finite resources are concentrated on high-impact cases. In October 2006, the OFT published a Competition Prioritisation Framework setting out new criteria for deciding if a case should be opened or an existing investigation continued.

20. The OFT began gathering information to help us gauge the impact on consumers of our enforcement actions. This included estimates of financial savings arising from past infringement decisions.
and the cost to the taxpayer of pursuing cases. We also conducted a survey of antitrust private practitioners to measure the deterrent effect of the UK competition regime.

21. This analysis will feed into our case prioritisation criteria to ensure that the OFT concentrate our resources in areas that benefit consumers most. We estimated that each year enforcement action leading to infringement decisions saves consumers £64m.

22. During the year, the OFT set up a new monitoring function to help identify the areas where we should target our resources. This work involves sifting through market intelligence supplied by stakeholders and Consumer Direct and assessing the likely impact of studies on consumer detriment and productivity.

23. The CC Council put in hand a comprehensive review of all the workings of the CC, how it was structured, how it does its job, what process and techniques its uses and how CC members and staff can best work together to become even more efficient and effective.

1.1.4 Review of Procedures and Analysis

24. The CC continued with its review of analysis in merger cases and of effectiveness of remedies (including a post case review of remedies in four merger cases, and piloting of streamlined approaches for merger inquiries). The CC published guidance for interim measures. It has established an internal system for peer review before publication of provisional findings, separate from its post investigation review. The CC has commissioned a report (to report in 2007/8) into the CC’s use of quantitative techniques and use of stock market data.

2. Changes to competition laws and policies, proposed or adopted

2.1 Summary of new legal provisions of competition law and related legislation

25. There was no new legislation introduced in the reporting period.

2.2 Other relevant measures, including new guidelines

• Private actions

26. In October 2006, the OFT hosted a workshop on private actions under competition law, bringing together around 60 leading figures in the competition field, including agency heads, lawyers, economists, academics, policymakers and representatives of business and consumer organisations. The workshop considered whether the UK needs additional measures to facilitate private actions and, if so, what lessons the OFT could learn from other jurisdictions. The OFT published a discussion paper on possible next steps in April 2007, and are holding an event in September 2007 to allow third parties to make their views known to us.

• ECN Model Leniency Programme

27. In September 2006, the annual meeting of Directors General of European competition authorities endorsed a model leniency programme developed by a working group of the European Competition Network co-chaired by the OFT. This marked a significant step towards the harmonisation of leniency programmes across the EU and will further facilitate the reporting of cross-border cartels in the EU.
• **OFT leniency and no-action guidance**

28. Following consultation, the OFT published final guidance on our handling of leniency and no-action applications in March 2007.

• **Guidance on procurement issues**

29. In January 2007, the OFT and the Office of Government Commerce published a joint guide for public sector procurers of construction services on achieving value for money through the competitive process. Written in the light of several enforcement actions against construction firms, the guide, ’Making competition work for you’, also highlights practical steps procurers can take to avoid falling victim to bid-rigging or price-fixing cartels.

• **Guidance on Interim Measures**

30. The CC published revised guidance for interim measures and template interim undertakings following a public consultation. Interim undertakings are generally required by the CC on all references of completed mergers in order to protect possible remedial action.

3. **Competition policy and law enforcement**

3.1 **Action against anticompetitive practices, including agreements and abuses of dominant positions**

• **Summary of activities**

31. In 2006-07, using powers under the CA98 and/or Articles 81 and 82, the OFT opened 829 cases, of which 20 involved possible cartel activity. Formal investigations were opened in nine cases where the OFT had reasonable grounds to suspect an infringement had occurred; six of these were potential cartel cases and two were launched under section 192 of the Enterprise Act. The OFT made two infringement decisions and the ORR made one infringement decision during the reporting period.

32. Following internal restructuring, from 1 October 2006 approximately 40 to 50 complaints a month were dealt with in a new area of the Office, which deals with external complaints and preliminary investigations. These complaints would have previously led to a case being opened under the Competition Act which has resulted in a fall in the number of cases opened compared to previous years.

33. The OFT conducted 14 on-site inspections in five separate investigations; 11 under section 27 of the Competition Act and three under section 28. The OFT also visited four business premises under the authority of criminal search warrants obtained under section 194 of the Enterprise Act.

34. The OFT, using powers under the Enterprise Act also issued 14 section 193 notices; one to a business and 13 to individuals, that required the immediate production of specified documents and/or the provision of specified information.

35. The OFT’s leniency programme allows fines to be reduced for businesses which ‘blow the whistle’ on cartels, and in certain conditions given total immunity to the first to come forward. In 2006-07, the OFT entered into leniency agreements with 19 undertakings in eight separate cases. Eight of these related to our on-going investigation of the UK construction industry. The OFT closed two other cases after securing changes in behaviour from the businesses involved.
Summary of Key Cases

Air passenger fuel surcharges

36. The OFT investigated allegations that certain major airlines, including British Airways and Virgin Atlantic, operating in the UK had engaged in price-fixing activities relating to the fuel surcharge element of the ticket price for long-haul passenger flights to and from the UK. Two parallel investigations were in progress: one against the implicated companies under the Competition Act and a second against specific individuals using our criminal powers under the Enterprise Act. In both cases the OFT liaised with the US Department of Justice, which launched a separate inquiry into the US aspects of the suspected infringement.

Construction cartel

37. Our two-year investigation into bid-rigging by construction companies in England uncovered evidence of unlawful practices in thousands of tenders with a combined estimated value approaching £3bn. During our inquiries, the OFT raided 57 companies and received 37 applications for leniency.

38. The OFT used digital evidence-gathering and forensic IT for the first time to retrieve information held on computers, along with forensic document analysis. This evidence related to bid-rigging activities such as ‘cover pricing’, where companies obtain a price from a competitor in the tender process which is not designed to win the contract but is intended to give the appearance of competition. In some instances we found evidence that compensation payments or ‘bungs’ were passed between competitors in exchange for a cover price.

39. To ‘fast-track’ our inquiries, in March 2007 the OFT offered to reduce the financial penalty for those implicated companies which had not applied for leniency but were willing to cooperate with the OFT in certain specific ways. The OFT also informed construction companies in England that, given the extent and quality of the evidence obtained, no further applications for leniency in this investigation would be considered.

Spacer bars

40. In June 2006 the OFT issued a decision finding that four companies had agreed to fix prices and share the market for aluminium spacer bars, which are used in the manufacture of double-glazing, and had breached Chapter I of the Competition Act. The infringement was brought to an early end as a result of our intervention. The OFT imposed total penalties on the parties involved of £1.38m, reduced to around £900,000 after leniency.

Independent Schools

41. In November 2006 the OFT issued a decision finding that an agreement between 50 of the UK’s fee-paying independent schools to exchange detailed fee information breached the Chapter I of the Competition Act. The findings marked the end of one of the OFT’s largest investigations, and resulted in total penalties of just under £500,000. The relatively low fine for each school took account of a number of exceptional features of the case, including the schools’ charitable status and predominantly the fact that they had agreed to make payments totalling £3m to a trust fund designed to benefit pupils who attended the schools during the relevant academic years.
42. In a novel approach to resolution, the OFT worked with a steering group, chaired by the Independent Schools Council, including senior governors nominated by the schools, on a proposed settlement. This was the first time the OFT had imposed penalties on charities and sent out a message that competition law applies to all businesses. The OFT also warned charities not to assume that financial penalties would automatically be lower in their case.

Scottish milk processing

43. The OFT sent a statement of objections to a number of Scottish milk processing dairies in November 2006. This set out our provisional finding that the companies had engaged in price-fixing by sharing pricing information and coordinating a series of price increases. The OFT also provisionally found they had colluded over arrangements not to compete for each other’s customers. The alleged infringement relates to the ‘middle ground’ market sector in Scotland, which includes customers such as schools, shops, cafes and hotels but excludes the big supermarkets and doorstep customers. At the end of the year, representations from the parties concerned were being considered.

English Welsh and Scottish Railway Limited (EWS)

44. ORR decided that EWS had infringed Chapter II of the Competition Act 1998 and Article 82 of the EC Treaty. The decision was based on our findings that EWS concluded contracts whose terms had the effect of excluding competitors from the market for coal haulage by rail and that it had also pursued discriminatory and predatory pricing practices in the same market.

45. EWS accepted ORR findings as set out in the infringement decision. EWS’s decision to accept ORR’s findings allowed ORR to resolve the case more quickly and effectively than would otherwise have been the case. ORR took this into account in setting the penalty of £4.1 million, to be imposed on EWS. ORR also issued certain directions to EWS and other parties to remove the contractual terms found to have an exclusionary effect.

- **Key Appeals**

Competition Appeal Tribunal appeals against Competition Act 1998 decisions

Construction cartel

46. Following an OFT decision in February 2006 that 13 companies had colluded to fix the price of contracts for flat-roofing and car park surfacing, appeals were lodged by two parties. Makers UK Ltd challenged both its liability and the penalty imposed, while Prate Ltd appealed the penalty only. Prate later requested, and was granted, permission by the CAT to withdraw its appeal.

47. In February 2007, the CAT unanimously dismissed Makers’ appeal against the infringement finding and, by a majority decision, dismissed its appeal against the level of penalty. This confirmed that the method the OFT uses to ensure that penalties act as a deterrent is appropriate, and that we were right to seek to impose substantial penalties for infringements of this nature.

London Metal Exchange (LME)

48. An OFT interim measures direction preventing the LME from extending the trading hours for its LME Select electronic trading platform was appealed in April 2006. The OFT lifted the direction the following month after new substantial material information on the market for trading non-ferrous metals came to light. LME subsequently withdrew its appeal but was awarded a proportion of its costs by the CAT in September 2006.
Casting Book

49. Our decision to close an investigation into an alleged boycott in the supply of celebrity merchandise was appealed in April 2006 by Casting Book Limited, who had filed the original complaint. The company argued that, in taking this action, the OFT had made a non-infringement decision which the CAT should review. However, the CAT ruled that the decision was not appealable and dismissed the case.

Stock check pads

50. The CAT found in our favour in a case relating to the supply of stock check pads, which are used by restaurants and similar establishments to record customer orders in the UK. The OFT imposed total penalties of around £2.1m before leniency on a number of companies for fixing prices for these pads and agreeing not to compete for each other’s customers. The CAT unanimously dismissed the appeal by Achilles Paper Group Limited and found that the penalty imposed upon it was appropriate.

Cityhook

51. Cityhook Limited, a submarine cable specialist, appealed against our decision to close our investigations on administrative priority grounds, into an alleged collective boycott and collective setting of wayleave fees by a number of telecommunications companies. In January 2007 the CAT ruled that the OFT had not taken an appealable decision in respect of our case closures, and that Cityhook’s appeal was inadmissible. The CAT earlier dismissed Cityhook’s application for disclosure of certain OFT internal documents relating to our decision.

Spacer bars

52. While there were no substantive appeals against our decision of June 2006 in this case, Double Quick Supplyline Limited and Precision Concepts Limited challenged the level of penalty the OFT imposed. The CAT dismissed the appeal in its entirety and awarded the OFT costs.

Mastercard

53. In June 2006, the CAT set aside, with our consent, our decision that the MasterCard UK Members Forum’s (MMF’s) historical arrangements for setting domestic interchange fees for purchases in the UK using UK-issued.

54. MasterCard credit and charge cards constituted an unlawful agreement; this decision had been jointly appealed by MMF, MasterCard International Incorporated, MasterCard Europe Sprl and the Royal Bank of Scotland Group. Visa Europe Limited and Visa UK Limited (Visa), whose own interchange fee arrangements were being investigated by us, intervened in the appeal. In a subsequent judgment the OFT were ordered by the CAT to pay the reasonable and proportionate costs incurred by the appellants and Visa since 31 March 2006.

55. Following the CAT judgment the OFT launched a fresh investigation into MasterCard’s current interchange fee arrangements and continued our investigation into Visa’s interchange fees. These investigations were subsequently extended to include debit cards.
• Court of Appeal

Ofcom Vs Floe telecom

56. The OFT intervened in support of a successful appeal by Ofcom against an order issued by the CAT. In line with Ofcom and OFT submissions, the Court of Appeal ruled that the CAT, on reaching a final judgment to set aside and remit a matter back to the regulator, does not have the power to order that a new investigation be carried out within a certain time. The judgment also contains helpful comments on the distinction between the role and functions of the OFT, concurrent regulators and the CAT.

Argos, Littlewoods v OFT and JJB v OFT

57. In October 2006, the Court of Appeal found in favour of the OFT in three linked cases relating to price-fixing in the toys and games market and in the supply of replica football kit. This was the first time it had ruled in cases of this nature under the Competition Act.

58. The court dismissed in full both Argos’s and Littlewoods’ appeals against liability for their part in price-fixing of certain toys and games, and JJB Sports’ appeal against liability for its price-fixing conduct in relation to replica football kit. Appeals by Argos, Littlewoods and JJB on the size of the penalty imposed by the CAT were also dismissed. The OFT was awarded its costs in defending these appeals. The three appellants were later refused leave to appeal these judgments to the House of Lords.

• House of Lords Appeal

Crehan Vs Inntrepreneur

59. The OFT was granted leave to intervene in a House of Lords appeal brought by Inntrepreneur Pub Company and others on points relating to the application of Articles 81 and 82. Inntrepreneur was seeking to overturn an earlier Court of Appeal ruling which, for the first time in the UK, had imposed damages for harm suffered as a result of an infringement of competition law. In its judgment of 19 July 2006, the House of Lords upheld the appeal and the original High Court judgment. It ruled, in line with the OFT’s submissions, that the obligation on national courts to avoid conflicting decisions did not require that they follow a EC decision when considering an issue concerning different parties on a different subject matter.

4. Mergers and Acquisitions

60. The OFT investigates completed and anticipated mergers above a certain size to assess their anticompetitive effects; the OFT then refers mergers to the CC, or accepts undertakings instead of a reference, where it believes they might result in a substantial lessening of competition (SLC). If referred, the CC decides whether the merger gives rise to an SLC and, if so, determines what remedy is appropriate. The CC also implements the remedy (either by the acceptance of undertakings or by making an order). Responsibility for monitoring remedies lies with the OFT.

61. A merger qualifies for investigation if the UK turnover of the business being acquired is over £70 million, or if the merger will create or enhance a 25 per cent share of supply of a particular product or service in the UK, or a substantial part of the UK.
4.1 Statistics

62. The OFT examined 131 mergers and merger proposals, 103 of these raised more complex competition issues; 20 of these cases were pre-notified.

63. The OFT referred 13 mergers to the CC, accepted undertakings in lieu of reference in six cases, and the CC completing and publishing reports on nine mergers. The markets investigated included railway freight haulage, farmed Atlantic salmon, healthcare waste treatment and disposal and live music venues.

64. The CC completed its investigation of and reported on 9 mergers, further 6 were ongoing at the end of the year. Of the 9, 5 were completed mergers (2 of which were cleared) and of the 4 proposed mergers, 2 were cleared.

4.2 Summary of key cases resolved by the OFT

• Boots plc/Alliance Unichem plc

65. This substantial UK merger in the pharmaceutical sector was conditionally cleared by the OFT, subject to the parties agreeing to divest around 100 pharmacies across the UK. These divestments were in local overlap areas where the merger reduced the number of competing pharmacies within a mile of each other from two to one, or from three to two.

66. In May 2006, the CAT upheld our decision following a challenge by Celesio AG. This was our first win in the CAT under the Enterprise Act merger control regime. Our decision and robust stance were broadly welcomed by the UK legal community. The case demonstrated the UK’s ability to resolve complex and problematic issues in first-phase merger control where parties are willing to engage constructively on remedy proposals.

• NASDAQ’s bid for the London Stock Exchange (LSE)

67. In January 2007, the OFT cleared the bid by The Nasdaq Stock Market, Inc. (NASDAQ) for control of the LSE; the fourth scrutinised proposed takeover of the LSE. Two earlier bids, by Deutsche Börse and Euronext, were referred to the CC, while a third, by Macquarie Bank of Australia, was cleared on competition grounds but was ultimately unsuccessful.

68. The OFT determined that NASDAQ did not materially compete with the LSE for listings by UK issuers. In UK equities trading, the OFT concluded that NASDAQ might be a potential entrant in the absence of a merger, but that a merged NASDAQ/LSE would not face a materially lower entry threat than the LSE does today. The OFT further concluded that, in this particular case, any merger impact in the markets for international listings by non-UK customers fell outside the substantive test for merger control. Our evidence, however, suggested that the proposed bid would not adversely impact these customers either. NASDAQ’s £2.7bn offer eventually expired without gaining majority support from LSE shareholders.

4.3 Summary of key cases referred by the OFT to the CC (CC report published in 2006/07)

• HMV Group plc and Ottakar’s plc

69. In December 2005, there were 190 Waterstone's bookshops and 141 Ottakar's bookshops in the UK.
70. The relevant product market was considered to be the retail sale of new books to consumers, although the CC believed it appropriate to assess separately the competitive effects of the proposed merger in terms of sales of deep-range titles and best-sellers. The CC found that the geographic market was no wider than the UK, although looked separately at local, regional and national aspects of competition. The CC considered that competitors within the market included all types of retailer, both specialist and generalist, and also including distance sellers including Internet retailers and book clubs.

71. The CC estimated that the combined UK market share of Waterstone's and Ottakar's in 2005 was around 24 per cent of all books and a somewhat higher proportion of the deep-range segment. After assessing the effects of the merger on local, regional and national competition we concluded that the proposed acquisition of Ottakar's may not be expected to result in an SLC within the market for the retail sale of new books (best-sellers or deep-range titles) in the UK.

- **Stericycle International LLC and Sterile Technologies Group Limited**

72. Before the merger, Stericycle and STG were the first and second largest suppliers, by revenue, of healthcare-risk waste services. Healthcare-risk waste is waste produced within the NHS or other healthcare settings that requires treatment before disposal, in the main either by high temperature treatment or by alternative technology treatment.

73. The CC concluded that the merger would give rise to an SLC in those areas where there were two or less constraining competitors for high temperature treatment services. The CC expected that this SLC would result in increased prices for high temperature treatment there. The CC also considered that competitive conditions in the healthcare waste collection market could be adversely affected since collectors could face higher costs for, and more limited access to, high temperature treatment facilities.

74. In the light of this conclusion, Stericycle submitted proposals to sell STG’s incinerators at Salford, Redditch and its incinerator and alternative technology plant at Wrexham. The CC agreed to give Stericycle the opportunity to pursue its partial divestiture proposal, but if it failed to secure a binding commitment from a purchaser within an agreed period, the CC would have the right to require the appointment of a divestiture trustee and to mandate the sale of part or all of STG in Great Britain. Undertakings to underpin these arrangements were accepted by the CC on 30 January 2007. The reference was brought to a close by the sale of the Wrexham, Redditch and Salford plants on 16 February 2007.

75. Implementation of the remedies was helped by the effective interim remedies put in place by the CC at an early stage in the inquiry, so as to ‘hold separate and maintain’ the merged businesses, prevent further integration and require the separation of management teams that had already been integrated. The interim remedies were the subject of an unsuccessful challenge before the CAT.

- **Joint Venture between Stagecoach Bus Holdings Limited and Braddell PLC in relation to megabus.com, Motorvator and Scottish Citylink**

76. This joint venture brought together the two main coach competitors on the Glasgow-Edinburgh, Glasgow-Aberdeen and Edinburgh-Inverness routes in Scotland. There are significant barriers to entry and other forms of transport act as only weak constraints, if any, on coach services on these routes. On services between Glasgow and Aberdeen, and on services between Edinburgh and Inverness, the CC concluded that the joint venture would result in higher fares and lower service levels than would otherwise have been the case. The parties agreed to sell particular services on these routes to restore competition.
77. In accordance with the CC’s practice in transport mergers, the CC considered point-to-point journey flows as relevant markets, while also having regard to wider network markets where relevant.

78. Following publication of the report, the parties to the joint venture agreed to give undertakings to sell the joint ventures Scottish Citylink-branded/megabus-branded services on the Saltire Cross to a purchaser approved by the CC.

- Pan Fish ASA and Marine Harvest NV

79. Pan Fish and Marine Harvest both farm Atlantic salmon as their principal activity. Within Europe, they both have substantial salmon farming activities in Norway and Scotland. Competition authorities in France, Norway, Spain and the US were also notified and received approval in all relevant jurisdictions. Approval was received from the Minister of Economic Affairs in France on 1 December 2006 subject to an undertaking from Pan Fish to dispose of Pan Fish Scotland.

80. The CC found that this acquisition would not significantly reduce competition nor give the merged company the opportunity to significantly raise prices or exploit its control of supply. For many customers, Norwegian salmon is viewed as a good alternative, which would constrain any attempt by the merged company to raise prices for Scottish salmon. The chances of the merged company being able to exploit those customers with a strong preference for Scottish salmon are small. The CC concluded that the anticipated merger may not be expected to result in an SLC in the market for the supply of European farmed Atlantic salmon in the UK.

- EC Merger Regulation (ECMR) and Casework

81. The ECMR gives the EC exclusive jurisdiction over mergers that exceed certain turnover thresholds. The OFT examined significant cases and provided the UK’s views to the EC and represented the UK at hearings and Advisory Committee meetings at which the EC’s draft decisions and policy notices were considered by member states.

82. The OFT made two requests under Article 9 of the ECMR to refer to the UK competition authorities a merger previously notified to the EC; the proposed acquisition by Veolia ES Holdings plc of Cleanaway Holding Limited and the completed acquisition by Aggregate Industries Limited of Foster Yeoman Limited.

83. Under Article 22 of the ECMR the OFT referred to the EC the anticipated acquisition by P.H.Glatfelter Company of certain assets of J.R. Crompton Limited and the acquisition by Thrane & Thrane of Nera Satcom AS.

84. The OFT considered a number of requests for pre-notification referral of a merger either from the UK to the EC (under Article 4(5)) or from the EC to the UK (under Article 4(4)). The OFT agreed to the referral to the UK of the following cases:

- completed acquisition by Inchcape plc of European Motor Holdings plc;
- completed acquisition by 02 UK Limited of Link Stores Limited; and
- anticipated acquisition by Govia Limited (through its wholly owned subsidiary, North London Orbital Railway Limited) of the London Rail Concession.
5. Market Studies and Investigations

5.1 Summary

85. In 2006-07 the OFT referred three markets to the CC for further investigation: Payment Protection Insurance, the Groceries market, and Airport services. The ORR also referred the market for the leasing of rolling stock for franchised passenger services to the CC.

86. The OFT also opened one market study and published reports in two other market studies during 2006-07.

87. During 2006-07 the CC reported on three market investigations: the Supply of Bulk Liquefied Petroleum Gas for Domestic Use; Home Credit; and Classified Directory Advertising Services. Work on four additional market investigations (Personal Account Banking Services in Northern Ireland, Payment Protection Insurance and Airports) was ongoing (the CC reported on its investigation into Northern Irish personal banking in May 2007).

5.2 Market Investigation References

88. Under the Enterprise Act, the OFT has the power to refer a market to the CC for further investigation where it believes there are reasonable grounds to suspect that a feature, or combination of features, of the market is or are preventing, restricting, or distorting competition. It is for the CC to decide if this is the case, and, if so, whether action should be taken.

89. If it makes an adverse finding, the CC has the duty to consider appropriate remedial action and has the power to impose remedies. When deciding upon the remedy, it may take into account the impact of the remedy on relevant customer benefits. As well as the ability to impose structural (including divestment) remedies, the CC may make recommendations to others of action they should take.

• Groceries Market

90. The OFT, following its public consultation which received over 1,200 responses in favour of a CC reference, referred the market for the supply of groceries by retailers in the UK to the CC in May 2006. The CC is due to publish a final report in early 2008.

91. The OFT investigation found that the planning regime acts as a costly barrier to entry, making it difficult for new stores to open and compete with those already in the market.

92. In addition the OFT found that big supermarkets have significant land holdings which could aggravate barriers to entry or otherwise harm consumers and in some instances, supermarkets have attached restrictive covenants when selling sites.

93. The OFT investigation concluded that there is evidence to suggest that the big supermarkets’ buyer power has increased, and that some aspects of their pricing behaviour, such as below-cost selling and price flexing could distort competition.

94. The CC is looking at a wide range of goods and services including food, drinks, toiletries, cleaning products and household goods; but excludes a number of goods and services including petrol, clothing, perfumes and gardening equipment. Issues within the market that the CC is considering include the behaviour of grocery retailers towards their suppliers, the structure of any local market for groceries, the operation of the planning regime as it affects grocery retailing and any conduct by grocery retailers, including any aspect of the acquisition, disposal, development or use of land, supply chain issues. The CC
published its Emerging Thinking in January 2007 and plans to publish the provisional findings for the investigation in autumn 2007.

- Payment Protection Insurance (PPI)

95. The OFT, after public consultation, referred the market for PPI in the UK to the CC in February 2007. The CC is due to publish its report in September 2008 (the statutory period for reporting expires in February 2009).

96. The OFT investigation which was launched in response to a super-complaint from Citizens Advice, concluded in October 2006 that consumers are getting a poor deal and often less protection than they think from the £5.5bn payment protection insurance market.

97. The OFT’s report found, among other things, that the point-of-sale advantage enjoyed by distributor’s means there is little competitive pressure at the key point at which consumers buy insurance; contributing to consumers not shopping around for the best deal.

98. The OFT also found that in some cases consumers also assume, or are led to believe, that taking out PPI will help with credit applications. The OFT recognised that the industry had been working with the Financial Services Authority (FSA) to address problems relating to sales standards. However, neither the OFT nor the FSA believed that these initiatives would resolve the broader competition issues we identified.

99. Issues that the CC is considering are those arising in the relevant retail (including customer behaviour, retail costs of providing PPI, competition between suppliers of PPI, barriers and the regulatory context) and wholesale (including customer behaviour, wholesale costs and competition between wholesalers) markets and issues arising from the relationship between different stages of the supply chain. The CC plans to publish the provisional findings for the investigation in autumn 2007.

- Airport Services

100. The OFT referred the supply of airport services by BAA to the CC in March 2007. The CC is due to publish a final report in December 2008 (the statutory reporting date is March 2009).

101. The OFT investigation, launched in June 2006, concluded that the current market structure does not deliver best value for air travellers in the UK, and that greater competition within the industry could significantly benefit passengers.

102. The OFT investigation found evidence of high charges and poor customer satisfaction. BAA owns Heathrow, Gatwick, Stansted and Southampton airports in England and Edinburgh, Glasgow and Aberdeen airports in Scotland. These airports have an annual turnover of £2bn and handle over 60 per cent of all air passengers in the UK.

103. The CC is carrying out the investigation concurrently with its quinquennial review into airport price controls at Gatwick and Heathrow. The regulatory review will govern how much BAA can charge airlines over the five year period beginning April 2008. The CC proposes to publish its emerging thinking in relation to the market investigation in early 2008.
• Review of passenger rolling stock leasing markets

104. ORR used its concurrent powers in deciding to refer the leasing of rolling stock for franchised passenger services to the CC for further investigation. The ORR referred the supply of leased rolling stock to the CC in April 2007 and the CC is due to publish a final report in September 2009 (the statutory reporting date is April 2009).

105. The decision followed a full public consultation on ORR’s competition assessment and the draft market reference. Following careful consideration of consultation responses, ORR remained of the view that certain market features are limiting competition and have the potential to lead to higher prices and a poorer quality of service than would otherwise be the case in a more competitive environment. ORR believed that a reference to the CC was an appropriate and proportionate response in the light of the competition concerns it identified; especially given the size and importance of these markets in the UK rail industry and the powers available to the CC to affect any remedy.

106. The issues that the CC is considering include the operation of the franchising regime, behaviour of rolling stock lessors and conduct of suppliers or customers. The CC plans to publish its emerging thinking in late 2007.

5.3 Other market studies

Internet Shopping

107. Internet retail sales account for approximately three per cent of household spending in the UK (over £21.4bn a year in total), with around 62,000 UK businesses selling online to households. Forecasts suggest that the typical online shopper will spend over £860 a year on purchases of goods in 2010, compared with £560 in 2005.

108. To examine the possible implications of this boom for consumers, the OFT launched a fact-finding study on internet shopping in April 2006. The study is exploring consumer confidence in this area and, in particular, whether changes to the regulatory regime are needed.

• Commercial use of public information

109. Improved competition in the supply of public sector information could benefit the economy by around £500m a year, the OFT reported in December 2006. Examples of public sector information include weather observations collected by the Met Office, family records held by The National Archives and mapping data collated by Ordnance Survey.

110. Our market study found that public sector information holders (PSIHs) are usually the only source for much of this information. Although some PSIHs make this available to businesses for free, others charge. A number also compete with businesses in turning the raw data into value-added products and services. This gives them an incentive to restrict access to information for which they are the sole provider.

111. The study recommended that PSIHs make as much public sector information as possible available for commercial use or re-use and, where they have a monopoly of supply, provide data to outside businesses on the same terms as to their own commercial operations. The OFT also called for the Office of Public Sector Information to monitor PSIHs more closely, and for enforcement and complaints procedures to be strengthened.
112. The OFT study recommended that the PPRS be reformed to deliver better value for money for the NHS and focus business investment on drugs that have the greatest benefits for patients.

113. The NHS spends about £8bn a year on branded prescription medicines. Our study, published in February 2007, identified a number of drugs whose prices are significantly out of line with patient benefits. These include treatments for cholesterol, blood pressure and stomach acid. In some cases drugs currently prescribed in large volumes are up to ten times more expensive than substitute treatments which deliver very similar benefits to patients.

114. The study concluded that the current ‘profit cap and price cut’ scheme, under which drugs companies are free to set their own prices within very broad profit constraints, should be replaced by a value-based pricing scheme which relates the price paid by the NHS to the therapeutic benefits that drugs bring to patients. The OFT estimated that this reform could release in the region of £500m per year that could be used more effectively, giving patients better access to medicines and other treatments they may currently be denied.

5.4 Completed Market Investigations

115. The supply of bulk liquefied petroleum gas for domestic use

116. Almost 150,000 households in the UK use domestic bulk LPG. It is a hazardous product and safety is a key concern to suppliers and was so in our consideration of this industry.

117. There are four suppliers with about 90 per cent of domestic bulk LPG in Great Britain – BP LPG UK, Calor Gas Limited, Flogas UK Limited (a subsidiary of DCC plc) and Shell Gas Limited; two of which are the only suppliers in Northern Ireland – Calor Gas Northern Ireland Limited and DCC Energy Limited (also a subsidiary of DCC plc).

118. The CC found that there were features of the markets for the supply of domestic bulk LPG which adversely affected competition in the UK. While some customers may negotiate competitive prices, it was concluded that the large majority of customers in the market were paying higher prices than would be the case if these features did not exist.

119. It was found that the rate of switching between suppliers was very low, even when savings could be made; aspects of pricing supported the view that competition was constrained. Selective discounts offered to customers in Great Britain reduced the potential rewards to competitors for attempting to win customers away from their current suppliers. The CC found barriers to expansion by smaller suppliers in the UK markets, which adversely affected competition. Switching costs created a barrier to expansion in that, in trying to win a customer, an entrant or smaller competitor would always be at a disadvantage.

120. The CC considered an effective and proportionate package of remedies to address the adverse effects on competition within the identified market which included: tank transfer, including a customer’s right to request tank transfer, standardisation of, and improved information on, the switching process; changes to customer contracts, and improved information on suppliers and their offers.

121. The CC also considered that, in Northern Ireland, the General Consumer Council for Northern Ireland should include information on the opportunities for customers to switch supplier in the information
it provides to energy customers in the context of the opening of the domestic mains gas and electricity markets to competition in 2007.

122. It was agreed that implementation of the above remedies would be by means of an Order with a period of up to nine months from the date of the Order for suppliers to ensure they are compliant.

- **Classified Directory Advertising Services**

123. The three largest directory providers (Yell, Thomson and BT) accounted for 98 percent of UK CDAS revenues. Yellow Pages had been subject to a price cap since 1996. Undertakings were initially given by BT, the then publisher of Yellow Pages, following an earlier inquiry by the CC’s predecessor. On disposal to Yell, Yell gave undertakings which largely constrained prices by a price cap and prevented Yell from publishing more than one directory in any area. An important development was the re-entry of BT in October 2002 by including a classified advertising section in its Phone Book.

124. The CC found a relevant product market for advertising services in major printed classified directories, characterised by strong brand image, high levels of usage and comprehensive business listings; online directories and Internet advertising were not part of this relevant market. The CC concluded that Yell has market power with the ability to set prices profitably at levels higher than they would be in a well-functioning market. The features identified by the CC having an adverse effect on competition included high concentration, high entry barriers, and the enhancement of Yell’s incumbency position by network effects. The CC also decided that if Yell were allowed unrestricted scope to produce second tier (local) directories, competition would be damaged.

125. The CC decided that remedies were appropriate and these included price controls and placing certain limitations on Yell’s publication of local ‘second tier’ directories.

- **Home Credit**

126. Home credit involves small loans, generally under £1,000; around 70% are for less than £500 and the average advance is around £300. Repayments, generally over a period of about a year or less, are typically collected in weekly cash instalments from the borrower’s home. The absence of competition between home credit lenders and the incumbency advantages enjoyed by established lenders meant that borrowers paid higher prices than they would pay in a competitive market. Borrowers in these circumstances paid at least £75 million a year more than they should. The CC’s remedies aimed to generate competition between existing home credit lenders and to make it easier for new lenders to supply the home credit customer base.

127. The investigation involved some 450 home credit lenders, all legitimately licensed businesses. Most lenders were companies engaging agents to collect repayments though over 200 sole traders or partnerships worked for them. The investigation included in-depth consideration of prices and the CC found that prices were high compared to cost of provision, and particularly high for those borrowers who settled early. The CC also found that profits in excess of capital amounted to at least £75m a year.

128. The CC concluded that borrowers’ insensitivity to prices and lenders’ failure to compete in any significant way on price were features preventing, restricting or distorting competition; so too, were incumbency advantages enjoyed by existing lenders and the factors contributing to the preservation of these advantages. These features taken together gave rise to an adverse effect on competition within the meaning of the Enterprise Act 2002.
129. The CC decided that remedies increasing price transparency and decreasing the information asymmetries between incumbent and other lenders were appropriate and these included the setting up of a website to enable comparison, sharing of information relating to borrowers through credit reference agencies, increase in the early settlement rebate and strengthening of requirements on statements. The remedies aim to develop greater price competition, to extend competition for home credit borrowers and to reduce significantly the detriment suffered by borrowers settling loans early. The CC made an Order in relation to the remedies in September 2007.

Northern Irish Personal Banking

130. The CC published its final report on its market investigation into Northern Ireland Personal Banking (referred by the OFT in May 2005) in May 2007. Current accounts are the most widely-held personal banking product in Northern Ireland. About 80 percent of households have access to a current account. Over 95% of personal current accounts are provided by 12 suppliers, 8 of which were clearing banks who earned income from providing such accounts in 2005 was £167m. The CC found that features having an adverse effect on competition were banks’ unduly complex charging structures and practices, their failure adequately to explain them and customers’ reluctance to switch to another bank.

131. The CC decided upon a package of remedies, including easy-to-understand terminology and description of personal current account services, explanation of levels of charges and interest rates and how and when they apply, better information, advance notice of charges and interest incurred giving customers at least 14 days’ notice before deducting charges and interest from their accounts and introducing improvements to the switching process to ensure customers who switch banks do not incur costs in doing so. The CC also recommended to BACS (the clearing house responsible for bulk clearing of electronic payments) a review of switching processes to identify and address any outstanding impediments to switching direct credits, debits and standing orders.

132. The CC plans to make an Order implementing the remedy late 2007, with the intention that the new measures will come into force in Northern Ireland in 2008 to coincide with likely changes throughout the UK from the current review of the Banking Code by the Banking Code Standards Board (BCSB) and from implementation of the Consumer Credit Act 2006.

5.5 Progress on completed market studies

Pharmacies

133. Discussions continued with the Department of Health (DH) on its review of entry restrictions for the community pharmacy market, which were the subject of an OFT report in 2003. Under current regulations, a new community pharmacy can only be established if a Primary Care Trust judges that it is ‘necessary or desirable’ for a given neighbourhood. In our talks with DH officials, we reiterated our view that lifting these controls would improve competition and reduce the price for over-the-counter medicines, saving consumers around £25-30m a year.

Private Dentistry

134. Private dental patients now have access to an independent complaints body under a scheme launched in May 2006 by the General Dental Council. The lack of independent redress was one of the main issues highlighted in our 2003 report on the private dentistry market. The new Dental Complaints Service provides mediation between the two parties in the event of a dispute. Where appropriate, it will recommend an apology, a refund of fees and/or a contribution by a dental practice towards the costs of
remedial treatment. The service expects to deal with around 2,000-4,000 complaints a year from across the UK.

- **Estate Agency Market**

135. The Consumers, Estate Agents and Redress Bill, introduced in Parliament in November 2006, implements a number of recommendations from our 2004 report on the estate agency market. The Bill contains measures to require estate agents to join an approved redress scheme. It also requires them to keep adequate records of their dealings with a client for six years, and allows trading standards officers to inspect these records. The Bill expands the circumstances in which the OFT can take regulatory action against estate agents.

- **Doorstep selling**

136. In September 2006, the Government announced its response to a public consultation launched in the wake of our 2004 report on doorstep selling. The Government proposed extending cancellation rights and cooling-off periods to solicited visits, requiring cancellation notices to be provided within contracts, and encouraging greater transparency on prices through improved self-regulation. Measures to implement the first of these proposals were included in the Consumers, Estate Agents and Redress Bill.

- **Review of Remedies**

137. The OFT is required to keep under review the actions taken in compliance with CC remedies, and to advise the CC if these are having their intended effect of making markets work better.

- **Condoms**

138. The CC released condom supplier LRC Products from undertakings arising from a 1994 report by its predecessor, the Monopolies and Mergers Commission (MMC). Our review found that the buyer power of retailers had increased significantly since the MMC report was published, leading to greater consumer choice and lower wholesale prices. These market changes meant that the original undertakings, under which LRC Products agreed not to enter into exclusive distribution agreements with wholesalers or retailers, were no longer needed.

- **Newspaper distribution**

139. The OFT launched a review of undertakings agreed by newspaper wholesalers in England and Wales, which include the Code of Practice for the supply of newspapers. The code was developed to remedy adverse effects identified in a 1993 MMC report. The review is considering whether the code, which supports the practice of publishers awarding exclusive territories to wholesalers, has proved effective or remains an appropriate remedy; it is also examining whether changes to the market require the undertakings to be varied or removed.

140. The review is being carried out in tandem with our analysis of the compatibility of newspaper and magazine distribution agreements with the Competition Act. A draft Opinion was published for consultation in May 2006 and a final Opinion will be published during the 2007–08 financial year. In December 2006, the OFT received a formal request to consider whether there are grounds to refer the market for the supply of newspapers and magazines in the UK; our decision on this will follow the findings on the code and Opinion.
Opium derivatives

141. The Government published its response to our review of undertakings given by MacFarlane Smith Ltd (MSL) concerning the supply of opium derivatives used in painkillers and other medicines. Our review had concluded that the present licensing policy, which seeks to protect UK production by limiting imports, allowed MSL, the UK’s principal supplier, to discriminate on prices and earn high levels of profit, driving up costs for the NHS.

142. The Government expressed concerns that increasing import quotas could threaten MSL’s ability to supply diamorphine, an opioid analgesic used extensively in the UK for palliative care. However, it recognised the potential effects on customers and competition of the issues we had raised and committed to analyse these further.

6. Resources of competition authorities

6.1 Annual expenditure

143. The OFT expenditure for 2006-07 on competition enforcement work was approximately €51 million. These figures exclude support services such as accommodation, IT services, HR, Finance etc, as well as a budget for litigation, which is budgeted to provide support to the OFT as a whole.

144. The CC expenditure for 2005-06 was approximately €29 million.

6.2 Number of employees

145. The OFT dedicated a total of 301 staff (41% of total staff) to competition enforcement activities in 2006-07.

146. Of the 301 staff dedicated to competition enforcement work 81 (27%) were lawyers, 84 (28%) were economists and the remaining 135 (45%) were other professionals.

147. At the OFT, of the 301 staff identified above, 120 (40%) were involved in enforcement against anticompetitive practices, and 35 (12%) were involved in merger review and enforcement.

148. At the end of March 2007, the CC had approximately 150 staff (the majority of which are professional staff including lawyers, economists, statisticians, accounting advisors and business analysts (174 at the end of March 2006).

149. The CC staff support the CC Members (generally a group of five Members considers a case). At the end of March 2007, there were 46 Members all of whom are part time.

150. Additionally, the Chairman and three Deputy Chairmen are members of the CC, together with the Chief Executive and two non-executive members are members of the Council (the strategic management board).
# ANNEX 1: SUMMARY OF CC MERGER REPORTS PUBLISHED FROM 1 APRIL 2006 TO 31 MARCH 2007

<table>
<thead>
<tr>
<th>Parties</th>
<th>Date of reference</th>
<th>Key timings</th>
<th>Conclusion and key issues</th>
</tr>
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</table>
| 1. HMV Group plc and Ottaker’s plc (Proposed) | 6 December 2005 | Report published 12 May 2006 | Clearance  
- Market for retail sale of new books at local, regional and national levels  
- Considerable public concern in relation to effects in Scotland |
- Market for own market carbonated drinks  
- High market concentration created by the merger of the two largest companies  
- Retailers bargaining power  
- Spare capacity of competitors |
- Joint venture relating to bus and coach services in Scotland  
- Point to point journeys as relevant market  
- Financial modelling analysing effects of merger on incentives to raise fares and reduce service  
- Barriers to entry increased  
- Divestiture of joint venture’s Scottish-Citylink-branded/megabus-branded services on the Saltire Cross |
| 4. EWS Railway Investments Limited and Marcroft Holdings Limited (Completed) | 6 February 2006 | Report published 12 September 2006 | SLC - Divestment of part of business  
- Market relating to railway freight (vertical merger involving relevant markets of freight haulage and freight wagon maintenance in Great Britain )  
- Barriers to entry and difficulty of EWS’ haulage competitors to move self supply of maintenance as supplied by Marcroft  
- SLC in freight haulage market  
- EWS agreed to sell a significant part of the Marcroft outstation business to create a viable competitor in maintenance business offering national coverage |
- Market for the supply of members’ agency services to active individual members of Lloyds  
- Three to two merger  
- Consideration of ‘failing firm’, co-ordinated effects |
- Healthcare risk waste treatment and disposal  
- Interim remedies were put in place at an early stage in the inquiry to ‘hold separate and maintain’ the merged businesses,
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<tr>
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<tbody>
<tr>
<td>prevent further integration and require the separation of management teams that had been integrated</td>
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<tr>
<td>Parties appealed the CC’s decision to put in place hold separate arrangements and the CC’s power to do so was upheld by the Competition Appeals Tribunal.</td>
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<td>An SLC was found in areas of the merger where there were two or fewer constraining competitors for high temperature treatment services</td>
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<td>A divestiture of three incinerators was implemented</td>
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<td><strong>7. Pan Fish ASA and Marine Harvest NV (Proposed)</strong></td>
<td>6 July 2006</td>
<td>Report published 18 December 2006</td>
<td>Clearance</td>
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<tr>
<td>The merger was also investigated in France, Norway, Spain and the USA.</td>
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<tr>
<td>Relevant market was for fresh farmed Atlantic salmon produced within Europe with EEA Geographic market.</td>
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<td>Consideration of short and long term strategies of withholding production</td>
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<td>Market for live music venues and promotion services</td>
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<tr>
<td>For market definition of venues, CC examined competitive constraints on each venue operated by the party. For promotion services, CC concluded the market was no wider than the UK.</td>
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<tr>
<td>Consideration of impact of recently developed and proposed venues</td>
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<td>The CC concluded that the acquisition could be expected to lead to an SLC in venues market through the loss of rivalry between the five main London venues of the merging entities leading to a worsening in the price and non-price factors on which they compete.</td>
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<tr>
<td>Divestment of part of the business (two venues) required.</td>
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<td>Market for UK harbour and terminal towage services</td>
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<tr>
<td>Relevant geographic market was local, restricted to individual ports</td>
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<tr>
<td>SLC through loss of competitor at Liverpool</td>
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<tr>
<td>The CC required divestment of either acquirer’s or target assets in Liverpool. The Merger was allowed to be completed since final undertakings providing for the continued separation of the Liverpool operations were accepted.</td>
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