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ANNUAL REPORT ON COMPETITION POLICY DEVELOPMENTS IN THE UNITED KINGDOM

-- 2011 --

This report is submitted by the United Kingdom to the Competition Committee FOR INFORMATION at its forthcoming meeting to be held on 13-14 June 2012.

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Executive Summary

1. Against the background of unprecedented international financial turmoil, especially in Europe, the UK has continued to face very challenging economic conditions, with low growth, fragile consumer confidence and high unemployment making life extremely tough for businesses and consumers alike. The UK's focus on driving competition, supporting economic growth and protecting vulnerable consumers is all the more important in such times.

2. During a period of uncertainty over the future of the competition regime in the UK, the Office of Fair Trading (OFT) and the Competition Commission (CC) have continued to deliver significant benefits for UK consumers. The OFT and CC annually estimate the benefits expected to flow to consumers from their work. Such estimates are inevitably imprecise and, because they are based only on the quantifiable impact of certain decisions, inevitably underestimate the dynamic and deterrence effects of the regime. The CC and the OFT estimated direct financial benefits to consumers of their work of £455 million for the market investigation regime and £127 million for mergers in 2010/11.¹ Figures for 2011/12 are still being calculated and will be published later in the year.

3. The forthcoming reforms to the competition regime in the UK, including the creation of the Competition and Markets Authority (CMA), entail significant changes for the OFT and CC. Key challenges for the coming year will be both to support a smooth transition to effective new institutional arrangements and to maintain the performance of the existing regime through a period of change.

4. Investigating anti-competitive behaviour has remained a priority this year. The OFT has carried a higher volume of competition law cases, with a peak of 22 civil cases open in the second quarter. Across its portfolio the OFT has sought to prioritise cases with a wider strategic significance, deterrence effect and precedent value. The OFT also launched an internal 'enforcement debate' to identify ways to improve enforcement across the board.

5. During the past year the OFT has examined 100 merger cases and referred nine of those to the CC for further assessment. It accepted undertakings in a further five cases. The OFT's merger work included high profile and complex cases, such as investigations into Kingfisher plc's acquisition of 30 former Focus DIY stores, Amazon.com Inc's acquisition of The Book Depository International Limited and a series of oil distribution cases. In 2011/12, the CC reported on four proposed mergers, all of which were cleared. The CC also reported on four completed mergers, three of which were cleared and one required full divestment of the acquired company.

6. Under the markets regime, the OFT published seven market studies and referred the audit, aggregates and private healthcare markets to the CC for further investigation. The OFT has also launched a new market study into dentistry. In addition to these newly referred investigations, the CC completed its market investigation into local bus services and progressed others into Movies on Pay-TV and BAA airports.

7. As the second-phase authority, the CC has no control over the number or type of inquiries that are referred. However, the CC continues to complete its work on matters referred to it quickly and efficiently and to a high standard. This is recognised by the CC's stakeholders. The results of its latest Stakeholder Perception Survey found overall satisfaction with the CC remains highly positive, with the CC

¹ These are annual estimates averaged over the three year period 2008/09 to 2010/11 and include the work done by both the OFT and the CC. Note, they are different from the OFT's share of the benefits from mergers and markets work presented in the OFT's annual Positive Impact note.

continuing to perform well on two important factors – thoroughness and transparency. The CC seeks to keep under review the effect of its specific merger decisions in the market. The most recent study (by Lear) of two recent merger clearance decisions found that price competition had increased in both markets following the mergers and that neither had led to any substantial lessening of competition.

8. The OFT and the CC have also pursued a number of joint working initiatives. They held a joint hypothetical merger seminar and worked together on the development of international best practices (including consulting on and adopting the best practice on co-operation between EU national competition authorities in merger review). The OFT and CC also engaged in mutual consultation on guidance and plans including the CC's revised market investigation guidelines.

9. In February 2012, John Fingleton announced that he will step down as the Chief Executive of the OFT later in the year, after seven years in the role. The Department for Business, Innovation and Skills is in the process of recruiting his successor and is also currently recruiting a Chair Designate for the CMA.

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

1.1 Government proposals for new legislation

10. Following a consultation, the Government has set out its plans for the future of the public competition regime in the UK. The reforms are designed to improve the robustness of decisions, to improve speed and predictability for businesses and to support the regime in taking forward high impact cases. This will be achieved by overhauling the institutional structure of the regime, amending some aspects of UK competition law and strengthening enforcement processes.

11. The Government has decided to create a new Competition and Markets Authority (CMA) that will bring the CC and the OFT's competition functions into a single organisation. The CMA will be independent of Government and constituted as a Non Ministerial Department. The CMA's Chief Executive and Board will be accountable directly to Parliament and the CMA will be required to consult on its planned work and set out at the end of the year how it has performed. It is expected that the transition to the CMA will be completed by April 2014.

12. The CMA will have a primary duty to seek to promote competition both within and outside the UK for the benefit of consumers. The CMA will have responsibility for cartel and antitrust cases, merger control, market studies and investigations, regulatory appeals and references, and competition advocacy.

13. The fundamental pillars of the UK competition regime will remain unchanged. The two-phase process for market and merger reviews will continue (with the use of independent panel members for the second phase stage being retained), and the Government has elected to retain an administrative process for Competition Act 1998 enforcement cases. The CMA will also retain some responsibility for business guidance, notably in the context of its market studies. Consumer enforcement powers will be retained for use where markets are not working well due to practices and market conditions that make it difficult for consumers to exercise choice.

14. The reforms will make a number of improvements to the markets, mergers and competition enforcement regimes. The changes encompass new statutory time limits for markets and mergers work, stronger investigatory powers and a new power for the Secretary of State to request the CMA to investigate public interest issues alongside competition issues in market inquiries and investigations. The legislation giving effect to these reforms will also enable enhancements to procedures for Competition Act 1998 cases, including introducing a greater degree of separation of decision making from investigation. Due process will be enhanced by ensuring that key case decisions will be taken by decision-makers independent from investigation teams. Alongside this, the reforms will provide for enhanced co-operation and

information sharing between the CMA and sectoral regulators, as well as with partners across the consumer regime. Finally, the Government plans to amend the criminal cartel offence in the Enterprise Act 2002 to remove the ‘dishonesty’ element and to exclude from the offence agreements made openly.

1.2 Other relevant measures, including new guidelines

1.2.1 OFT Competition law compliance guidance

15. In June 2011 the OFT published new guidance for businesses on competition law compliance that included specific advice for directors, general guidance for all businesses, a quick guide to competition law compliance and a short film.

16. These resources build on the findings of the OFT's research report into the Drivers of Compliance and Non-Compliance with Competition Law published in May 2010, which identified the need for a risk-based approach to competition law compliance [www.of.gov.uk/OFTwork/competition-act-and-cartels/competition-law-compliance/].

1.2.2 OFT Consultation on updated leniency and penalties guidance

17. In October 2011 the OFT launched a consultation on two revised guidance documents, setting out proposals to update its approach to financial penalties and to awarding leniency in competition cases.

18. In its draft penalty guidance, the OFT proposed a number of changes to the way it sets penalties in competition cases. These are designed to ensure that the OFT sets fines that are sufficient to deter companies from engaging in anti-competitive activity, but that are also fair and proportionate.

19. In parallel, the OFT is consulting on its draft leniency guidance. This has been updated to reflect the OFT's experience of leniency since the last revision to this guidance in 2008.

20. Final versions of both guidance documents will be produced after considering the views expressed by respondents to the consultation. The penalty guidance will require approval by the Secretary of State for Business, Innovation and Skills [www.of.gov.uk/news-and-updates/press/2011/116-11].

1.2.3 OFT Guidance for UK public bodies on competition law

21. Public bodies must comply with the UK and EU competition law prohibitions on anti-competitive agreements and abuse of a dominant position if and when they engage in 'economic activity', as opposed to carrying out non-economic, wholly social functions or exercising public powers.

22. To that end, in December 2011 the OFT published a practical guide to assist public bodies in determining when their activities may be subject to competition law, so that they can ensure that their activities remain compliant with that law [www.of.gov.uk/OFTwork/competition-act-and-cartels/guidance-public-bodies].

1.2.4 OFT Consultation on Competition Act procedures guidance

23. In March 2012, the OFT launched a consultation on proposals to strengthen its Competition Act 1998 (CA98) decision-making processes, through introducing a new system of decision-makers who are separate from investigation teams.

24. To improve the speed and robustness of investigations, as well as increase engagement with the parties involved, the OFT is making further enhancements to its processes for handling CA98 investigations including:

- More interactive oral hearings, to provide greater opportunity for dialogue between parties to an investigation and the decision-makers on the case.
- More 'state of play' meetings, to update parties on the OFT's progress in an investigation and provide a forum for parties to make their points of view known during the investigation.
- A new ability for parties to make representations on key elements of draft penalty calculations, giving parties an opportunity to comment ahead of the final decision being taken.
- New arrangements for internal checks and balances within the OFT, involving scrutiny by lawyers and economists who are not part of the investigation team.
- Publishing case opening notices and case-specific administrative timetables on the OFT website to improve transparency of ongoing CA98 investigations.

25. The OFT also announced it would be extending the trial of its Procedural Adjudicator role for a further year, to March 2013, with an expanded remit, including responsibility for chairing oral hearings in CA98 cases and reporting to the decision-makers on whether the parties' procedural rights have been respected (www.of.gov.uk/news-and-updates/press/2012/23-12).

1.2.5 CC Proposed new Merger Procedural Guidelines

26. In April 2011, the CC invited comments on its consultation for new Merger Procedural Guidelines. The guidance describes the main stages of a merger inquiry and outlines the key interactions which the CC has with parties and their advisers in the course of a typical inquiry.

27. The CC is working on finalising the new Guidelines and expects to publish them in the next few months [www.competition-commission.org.uk/assets/competitioncommission/docs/2011/consultations/110426_mergers_procedural_guidance_final_draft_publishing.pdf].

1.2.6 CC Consultation on revised Market Investigation Guidelines

28. The CC decided in early 2010 to revise its market investigation guidelines, which had been drafted in 2003 before any investigations had been referred under the then new framework. The revised guidelines take account of the CC's subsequent experience of carrying out such investigations (14 have now been referred).

29. In March 2010 the CC invited initial views on various questions from major stakeholders. In April 2011, the CC published for comment specific parts of its revised guidelines (role of market investigations, the use of theories of harm, remedies and market investigation procedures). A public consultation on the full draft guidelines is expected to be conducted in the summer of 2012 (http://webarchive.nationalarchives.gov.uk/20111108202701/http://www.competition-commission.org.uk/our_role/ms_and_fm/cc3_review.htm).

2. Enforcement of competition laws and policy

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

2.1.1 *Dairy*

30. In August 2011, the OFT issued a decision following its dairy products retail pricing investigation, imposing fines totalling £49.51 million on four supermarkets and five dairy processors.

31. The OFT concluded that the supermarkets and dairy processors infringed the Competition Act 1998 by co-ordinating increases in the prices consumers paid for certain dairy products in 2002 and/or 2003. This co-ordination was achieved by supermarkets indirectly exchanging retail pricing intentions with each other via the dairy processors - so called A-B-C information exchanges. The OFT found that three infringements were committed. Not all companies were involved in all three infringements.

32. Most parties entered into early resolution agreements and so secured reductions in their fines. The OFT's decision is currently being appealed by one supermarket in the Competition Appeal Tribunal (www.of.gov.uk/news-and-updates/press/2011/89-11).

2.1.2 *E-Books*

33. Following a significant number of complaints, the OFT opened an investigation into whether arrangements that certain publishers have put in place with some retailers for the sale of e-books may breach competition rules. However, in December 2011 the OFT decided to close its investigation on grounds of administrative priorities, in particular because the OFT believed, following discussions with the European Commission, that the Commission was well placed to arrive at a comprehensive resolution of this matter and would do so as a matter of priority.

34. The OFT will continue to cooperate closely with the European Commission on this matter to help secure the best outcome for UK consumers (www.of.gov.uk/OFTwork/competition-act-and-cartels/ca98/closure/e-books).

2.1.3 *Motor insurance*

35. In December 2011 the OFT accepted formal commitments from six insurance companies and two IT software and service providers to limit the data they exchange between them. An OFT investigation identified an increased risk of price coordination among motor insurers using a specialist market analysis tool that allowed insurers to access not only the pricing information they themselves provided to brokers, but also pricing information supplied by other competing insurers.

36. The OFT warned the firms that, because insurers were able to access information about their competitors' future pricing intentions, the information exchanged through the market analysis tool raised competition law concerns, in particular that it could potentially be used to coordinate on price.

37. The formal commitments addressed these concerns by ensuring that the companies would exchange pricing information through the analysis tool only if that information meets certain principles agreed with the OFT. These principles require the information, if less than six months old, to be anonymised, aggregated across at least five insurers and already 'live' in broker-sold policies (www.of.gov.uk/news-and-updates/press/2011/129-11).

2.1.4 School suppliers

38. In December 2011 members of a group of school suppliers in the public sector gave voluntary assurances to the OFT regarding the way they compete for business from schools in England.

39. The OFT approached members of the Pro5 group of Public Sector Buying Organisations earlier in the year following a complaint which highlighted possible competition concerns about the way in which they marketed their goods and services to schools.

40. The assurances coincided with new OFT guidance to help public sector bodies understand when and how competition law applies to them (www.of.gov.uk/news-and-updates/press/2011/130-11).

2.1.5 Airline fuel surcharges

41. In April 2012 the OFT announced its decision that British Airways (BA) and Virgin Atlantic Airways (VAA) engaged in anti-competitive practices in relation to the pricing of passenger fuel surcharges, and imposed a fine of £58.5 million on BA. VAA brought the matter to the OFT's attention and, under the OFT's leniency policy, was not fined.

42. The OFT concluded that between August 2004 and January 2006, BA and VAA co-ordinated their surcharge pricing on long-haul flights to and from the UK through the exchange of pricing and other commercially sensitive information.

43. The £58.5 million fine imposed on BA was a reduction from the level of fine originally agreed between the OFT and BA in August 2007 as part of an early resolution agreement. The fine was reassessed following the issue of a Statement of Objections in November 2011 in light of a number of factors. These included legal developments regarding penalty setting for competition law infringements and the fact that the overall value added to the OFT's investigation by BA's co-operation was greater than had been anticipated at the time of the original agreement (www.of.gov.uk/news-and-updates/press/2012/33-12).

2.1.6 Hotel online booking

44. In September 2010, the OFT launched a formal investigation into suspected breaches of competition law in the hotel online booking sector, in particular in relation to arrangements between hotels and online travel agents.

45. The OFT continues to consider this matter as an administrative priority and is pursuing the investigation further.

46. At this stage of the investigation, the OFT has not yet concluded whether it considers the law has been infringed. The OFT anticipates that it will be in a position to decide whether it will proceed to issuing a Statement of Objections by the end of June 2012 (www.of.gov.uk/OFTwork/competition-act-and-cartels/ca98-current/online-booking/).

2.2 Competition Appeal Tribunal judgments

2.2.1 Tobacco

47. In December 2011 the Competition Appeal Tribunal (CAT) allowed appeals against the OFT's 2010 Tobacco Decision and quashed the Decision in relation to the six appellants. The CAT judgment makes clear that it does not address any of the substantive issues raised in these appeals, stating: 'We have not come to any view as to whether the agreements described in the Decision or the restraints that the OFT

now alleges were entered into would, if proven, amount to infringements of the Chapter 1 provision [of the Competition Act 1998].'

48. The OFT considered it important to investigate fully concerns around the pricing practices of the parties in this case and to make a decision about them. Despite the disappointing outcome in the particular facts and circumstances of this case, the OFT will continue to pursue high impact enforcement cases, including taking difficult or highly complex cases of this type that test the law.

49. The OFT issued the following statement following the CAT's judgment: www.of.gov.uk/news-and-updates/press/2011/134-11

2.3 *Mergers and acquisitions*

50. A merger qualifies for investigation if the UK turnover of the business being acquired is over £70m, 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. The OFT investigates completed and anticipated mergers above a certain size to assess their anticompetitive effects; where the OFT believes they might result in a substantial lessening of competition (SLC), it refers mergers to the CC, or accepts undertakings instead of a reference. The CC conducts in-depth investigations and decides whether a merger should be prohibited, allowed to proceed under conditions or cleared.

2.3.1 *Statistics on number, size and type of mergers notified and/or controlled under competition laws*

51. In 2011-12, the OFT examined 100 merger cases referring nine to the CC. The OFT's reference test was met in a further 11 cases. Of these, OFT accepted undertakings in lieu of a reference to the CC in three cases during the year (plus an additional two carried over from the year before), and cleared three cases on the basis that the relevant markets were not of sufficient importance to justify a reference (the 'de minimis' exception). Negotiations for undertakings in lieu of a reference are still ongoing in five further cases.

52. The CC reported on eight mergers during the year. The CC was referred nine mergers by the OFT and one by the Secretary of State for Business, Innovation and Skills. Three of these references were subsequently cancelled and three merger investigations are ongoing.

- Unilever/Alberto Culver Company

In June 2011 the OFT accepted undertakings from Unilever in relation to its completed acquisition of hair and personal care products manufacturer, the Alberto Culver Company.

The OFT concluded that the acquisition would or may have given rise to a substantial lessening of competition in respect of bar soaps in the UK resulting from the loss of a strong competitive constraint on Unilever's Dove brand. To address this concern, Unilever offered to divest the bar soaps business of Alberto Culver that includes the Cidal, Wright's and Simple brands. Unilever successfully secured an 'upfront' buyer, Lornamead, within the required timescales. As a result, the merger was not referred to the CC. www.of.gov.uk/news-and-updates/press/2011/66-11

- BATS Trading Limited/Chi-X Europe Limited

In June 2011 the OFT referred the anticipated acquisition by BATS Trading Limited of Chi-X Europe Limited to the CC for further investigation.

The merger involved the second and third largest platforms for the trading of UK listed equities, and would reduce the number of trading platform operators with meaningful shares (that is, above one per cent) from three to two.

In November 2011 the CC cleared the merger. The CC found that customers would have the power to prevent any attempt by the merged company to raise trading fees or worsen service quality, by taking, or threatening to take, their business elsewhere or even potentially sponsoring new entry. www.competition-commission.org.uk/our-work/directory-of-all-inquiries/bats-trading-chix-europe.

- Headland Foods Limited/Kerry Foods Limited

In July 2011 the OFT referred the completed acquisition of the frozen ready meals business of Headland Foods Limited by Kerry Foods Limited to the CC for further investigation.

Before the merger in January 2011, Headland and Kerry were the two largest suppliers of frozen ready meals to UK retail customers such as supermarkets.

In December 2011, the CC cleared the merger concluding that several customers had successfully found alternative suppliers since the merger in response to proposed price rises from Kerry/Headland—and at prices similar to those they had been paying prior to switching. The CC concluded that the existing and potential alternatives offered by other suppliers will ensure that the merger does not lead to a substantial lessening of competition (SLC) and that customers are unlikely to suffer from significantly higher prices or reduced choice as a result of the acquisition. www.competition-commission.org.uk/our-work/directory-of-all-inquiries/kerry-foods-headland-foods

- Acergy/Subsea 7

In August 2011 the OFT accepted undertakings to address the competition concerns arising from the completed acquisition of Subsea 7 Inc by Acergy S.A. (since renamed Subsea 7 S.A.).

The merger raised competition concerns in the North Sea area relating to the provision of small diameter rigid pipelay services alone, and projects which required the provision of both small diameter rigid pipelay and diving services. The OFT found that the sale of the Acergy Falcon pipelay vessel would restore pre-merger levels of competition. As a result, the merger was not referred to the CC. www.of.gov.uk/news-and-updates/press/2011/91-11

- Stericycle, Inc/Ecowaste Southwest Limited

In August 2011 the OFT referred the completed acquisition by Stericycle, Inc (Stericycle) of Ecowaste Southwest Limited (Ecowaste) to the CC for further investigation. Pre-merger, the parties competed in the collection, treatment and disposal of healthcare risk waste in the wider area around Bristol.

In March 2012 the CC concluded that the merger would lead to a substantial lessening of competition in the collection, treatment and disposal of healthcare risk waste for large quantity and small quantity generators of such waste in the City of Bristol, Bath & North East Somerset, and South Gloucestershire resulting in higher prices and lower service levels for these customers than would have been the case in the absence of the merger.

The CC announced that it would require Stericycle to sell Ecowaste to address the competition concern it had identified.

The CC had also considered other remedy options proposed by Stericycle as alternatives to a full divestment to address the loss of competition. However, it concluded that a full sale of the Ecowaste company would be the only effective remedy.

Stericycle later brought a judicial review challenge against the CC's decision as to remedies (see section 2.2.2 below). www.competition-commission.org.uk/our-work/stericycle-ecowaste

- GB Oils Limited/Pace Fuelcare Limited

In September 2011 the OFT accepted an offer by GB Oils Limited to divest oil distribution operations in the Isle of Wight to remedy competition concerns raised by its acquisition of Pace Fuelcare Limited. The OFT was concerned that the merger would have led to the creation of a monopoly for the supply and distribution of heating oils and transport fuels on the Isle of Wight. As a result of the divestments, which resolved competition concerns, the merger was not referred to the CC. www.of.gov.uk/news-and-updates/press/2011/104-11

- Anglo American / Lafarge

In September 2011, the OFT referred the proposed UK construction materials joint venture between Anglo American PLC and Lafarge S.A. to the CC for further investigation.

The proposed joint venture involved overlaps between the parties' activities in a number of product markets, at local, regional and national levels. In addition, there were vertical supply relationships between the parties' activities.

In May 2012, the CC announced that the parties would be required to sell a significant portfolio of operations, paving the way for entry by a new competitor into the UK cement market, before their proposed construction materials joint venture can go ahead. In its final report the CC expressed concern that the joint venture would increase the danger of coordination in the market for bulk cement and would reduce competition in local and national markets for other products including aggregates, asphalt and ready-mix concrete. www.competition-commission.org.uk/our-work/anglo-american-lafarge

- Alpha Flight Group Limited/LSG Lufthansa Service Holding AG

In October 2011 the OFT referred the anticipated joint venture between Alpha Flight Group Limited (Alpha) and LSG Lufthansa Service Holding AG (LSG) to the CC for further investigation.

The companies were major UK suppliers of in-flight catering to the airline industry, providing both hot meals and light snacks and related logistics for passenger flights in and out of the UK.

In March 2012 the CC announced its decision to clear the transaction. Airlines' catering requirements vary depending on whether they are long-haul or short-haul carriers with further differences between premium and economy passengers. Consequently, the CC looked at how the joint venture would affect competition in a number of different market segments, including distinguishing between Heathrow Airport, due to its larger number of long-haul flights, and other airports in the UK.

For the most frequent long-haul airlines out of Heathrow (excepting BA), the joint venture would reduce the number of 'traditional' suppliers to two. However, the CC found that entry by a rival with a different business model was a sufficiently credible alternative to ensure adequate competition among three suppliers when these airlines are tendering for business.

Elsewhere at Heathrow and other airports, the CC concluded that the ability to choose between a number of other suppliers and the less complex catering requirements of short-haul flights meant that airlines had several alternatives to the joint venture. The position of airlines was also strengthened by the increasing tendency for different parts of the supply chain—for example, food preparation and delivery—to be supplied by different companies, which enabled other companies to enter the market and increased airlines' options. www.competition-commission.org.uk/our-work/directory-of-all-inquiries/alpha-flight-group-limited-lsg-lufthansa-service-holding-ag-merger-inquiry

- Kent Messenger Group/Northcliffe Media Limited

In October 2011 the OFT referred the anticipated acquisition by Kent Messenger Group (KMG) of several newspapers from Northcliffe Media Limited to the CC for further investigation.

The merging parties publish the only local weekly newspapers in seven local areas in East Kent. The OFT's investigation concluded that the monopoly of local newspapers that would result in these areas risked costlier advertising for businesses and higher cover prices for readers.

In November 2011 the transaction was abandoned and the CC subsequently cancelled its inquiry.

www.offt.gov.uk/news-and-updates/press/2011/111-11

www.competition-commission.org.uk/media-centre/latest-news/2011/Nov/newspaper-merger-inquiry-formally-cancelled

- Princes Limited/Premier Foods Group Limited

In December 2011 the OFT accepted undertakings offered by Princes Limited to address the competition concerns arising from its completed acquisition of the canning business of Premier Foods Group Limited. The Fray Bentos brand and its manufacturing assets were sold to Baxters Food Group Limited to resolve competition concerns raised by the merger. As a result, the merger was not referred to the CC. www.offt.gov.uk/news-and-updates/press/2011/139-11

- Rontec Investments LLP/Total Downstream UK plc

In January 2012 the OFT accepted undertakings offered by Rontec Investments LLP in relation to its proposed acquisition of certain petrol forecourts, stores and other assets from Total Downstream UK plc, Total UK Limited and their affiliates.

The undertakings addressed the OFT's competition concerns regarding the retail supply of fuel in the Haverfordwest area. As a result the merger was not referred to the CC.

www.offt.gov.uk/news-and-updates/press/2012/03-12

- IAG/bmi

The proposed acquisition International Airline Group (IAG) of bmi from Lufthansa generated a significant level of concern in the UK especially in Scotland, the North West of England and Northern Ireland.

This deal qualified for investigation by the European Commission under EU merger rules. The OFT worked closely with the Commission during the course of its inquiry to ensure that the interests of British consumers were protected. This resulted in IAG offering a remedy package which included, among other things, the obligation to divest multiple slots at London Heathrow to be used for routes to and from Edinburgh and/or Aberdeen, and other measures to protect

Scottish travellers who use London Heathrow for international flight connections. <http://www.offt.gov.uk/news-and-updates/press/2012/13-12>

- Linergy /Ulster Farm

In March 2012 the OFT referred the anticipated acquisition by Linergy Limited of Ulster Farm By-Products Limited to the CC for further investigation. Linergy and Ulster Farm are two of the three renderers of animal by-products in Northern Ireland.

- The OFT's investigation concluded that there is a realistic prospect that the merger would result in a substantial lessening of competition in relation to the processing of certain categories of animal by-products and the processing of fallen stock in Northern Ireland. Soon after the reference to the CC the parties abandoned the transaction and the CC subsequently cancelled its inquiry. www.offt.gov.uk/news-and-updates/press/2012/18-12
- Other merger cases pending CC final decision
 - South Staffordshire Plc / Cambridge Water PLC merger inquiry (referred by OFT January 2012)
 - VPS Holdings Limited / SitexOrbis Holdings Limited (referred by OFT March 2012)
 - DCC/Rontex (referred by OFT April 2012)
 - McGill's Bus Services Limited / Arriva Scotland West Limited (referred by OFT April 2012)

2.3.2 *Judicial Review Challenges to CC Merger Decisions*

- SRCL Limited v CC

On 16 April 2012, SRCL Limited brought a judicial review application in respect of the CC's decision in its report dated 21 March 2012 which required SRCL to sell Ecowaste Southwest Limited, a company it had acquired in 2011. The CC had found that the merger would lead to a substantial lessening of competition (SLC) in the collection, treatment and disposal of healthcare risk waste for large quantity and small quantity generators of such waste in the City of Bristol, Bath & North East Somerset, and South Gloucestershire. The CC had considered alternative remedy proposals offered by SRCL but concluded that selling Ecowaste Southwest would be the only effective remedy capable of addressing the SLC. The Competition Appeal Tribunal gave its judgment on 24 May 2012 which dismissed SRCL's application. www.catribunal.org.uk/238-7621/Judgment.html

3 **Summaries or references to new reports, market investigations and studies on competition policy issues**

3.1 *Selected OFT market studies*

3.1.1 *Organic waste*

53. In September 2011 the OFT published its market study on the treatment of organic waste in England and Wales. The study followed a request from the UK Water Services Regulation Authority (Ofwat), with whom the OFT worked closely throughout the study.

54. The study identified a number of barriers to competition related to aspects of economic, environmental and planning regulation, and to the apparent corporate culture of some water and sewerage companies.

55. The OFT's report made a range of recommendations aimed at promoting competition in order to help drive efficiency and innovation in the sector. The recommendations also propose changes to the economic regulation of water and sewerage companies to foster efficiency and help create a level playing field between them and other suppliers of organic waste treatment (www.of.gov.uk/news-and-updates/press/2011/103-11).

3.1.2 Audit market

56. In October 2011 the OFT referred the market for the supply of statutory audit services to large companies in the UK to the CC for further investigation. The OFT had been concerned for some time that the audit market is highly concentrated, with low levels of switching and substantial barriers to entry.

57. In 2010, the four largest firms (PwC, KPMG, Deloitte and Ernst & Young) earned 99 per cent of audit fees paid by FTSE 100 companies. Between 2002 and 2010, the average annual switching rate among FTSE 100 companies was only 2.3 per cent.

58. Before provisionally deciding to refer the market to the CC, the OFT held a number of meetings with audit service providers, customers and regulatory bodies. One of the issues considered by the OFT during these meetings was the potential for overlap with parallel work ongoing at a European level. However, the nature, content and timing of EU legislation was not settled and the OFT believed that there were a number of important inputs that the CC might make during the legislative process. The OFT also believed that a CC inquiry had the potential to address UK-specific competition concerns that may not be within the scope of the EU's work (www.of.gov.uk/news-and-updates/press/2011/115-11).

3.1.3 Aggregates, cement, and ready-mix concrete

59. In January 2012 the OFT referred the aggregates, cement and ready-mix concrete markets in Great Britain to the CC for further investigation.

60. The OFT had concerns regarding structural features of these markets and reasonable grounds for suspecting that these were preventing, restricting or distorting competition. Features the OFT identified in its study include high barriers to entry in aggregates and cement, high concentration (five major players accounting for upwards of 90 per cent of the cement market, 75 per cent of aggregates sales and around 70 per cent of ready-mix production), as well as multiple contacts and information exchanges across the markets, with major firms supplying each other with both aggregates and cement, and engaging in joint-ventures and asset swaps. Moreover, the OFT noted that the major firms are vertically integrated across aggregates, ready-mix concrete and cement markets (www.of.gov.uk/news-and-updates/press/2012/02-12).

3.1.4 Private healthcare

61. In April 2012 the OFT referred the market for privately funded healthcare services in the UK to the CC for further investigation.

62. The OFT was of the view that the private healthcare market could work better for patients, and that there were reasonable grounds for suspecting that there are features of the market that prevent, restrict or distort competition.

63. Features the OFT identified in its study included a lack of easily comparable information available to patients, GPs or health insurance providers on the quality and costs of private healthcare

services, a limited number of providers as well as barriers to new competitors entering and being able to offer private patients greater choice (www.offt.gov.uk/news-and-updates/press/2012/26-12).

3.2 *Research papers/studies*

3.2.1 *Consumer Behavioural Biases*

64. In May 2011 the OFT published a research paper entitled *Consumer Behavioural Biases in Competition* in association with Steffen Huck and Jidong Zhou (University College London). This report examines the implications of consumer behavioural biases for firms' decisions and hence for competitive equilibria. The report looks at the key implications for consumer and competition policy in particular to understand how and when competitive equilibrium may change for the worse (www.offt.gov.uk/shared_offt/research/OFT1324.pdf).

3.2.2 *Conjectural Variations*

In October 2011 the OFT published a research paper entitled *Conjectural Variations and Competition Policy: Theory and Empirical Techniques* which was commissioned by the OFT from RBB Economics. The report questions whether incorporating firms' conjectures of how their rivals will react to price changes will impact competition policy. Specifically the report looked how firms' conjectures impact on (i) unilateral merger analysis, (ii) coordinated merger analysis and (iii) empirical estimates of the degree of competition (www.offt.gov.uk/shared_offt/research/CV_Competition_Policy.pdf).

3.2.3 *Competition and Growth*

65. In November 2011 OFT published an economic discussion paper entitled *Competition and Growth*, which identified ways in which competition interventions can help stimulate and support innovation and growth. The paper provides evidence of the links between competition and growth, considering how competition can contribute to the better utilisation of capital, labour and natural resources, and to increased innovation and better management, and highlights the role of government and competition authorities in ensuring that these links are maximised (www.offt.gov.uk/shared_offt/economic_research/oft1390.pdf).

3.2.4 *Deterrence*

66. In December 2011 the OFT published a report on competition compliance and deterrence resulting from the UK competition regime. The study was conducted by London Economics and included a survey of more than 500 large companies and 300 SMEs, as well as a small survey of specialist competition advisers in law firms. The research shows that sanctions and enforcement in the UK have a substantial deterrent effect. For each completed competition enforcement case, up to 40 potential competition law infringements are deterred (www.offt.gov.uk/news-and-updates/press/2011/131-11).

3.2.5 *Remote communities*

67. In February 2012 OFT launched a fact-finding review to understand more about the challenges facing consumers and businesses in remote communities across the UK. Prices of many goods and services are frequently higher in remote communities. The OFT is seeking to explore this and other issues with communities and businesses in remote areas, with the aim of improving understanding of how consumer or competition law can help tackle them (www.offt.gov.uk/news-and-updates/press/2012/09-12).

3.2.6 *Evaluation of CC's past cases*

68. The CC seeks to keep under review the effect of its specific merger decisions in the market. In 2011, the CC asked Lear to undertake a study of past decisions reached on two merger investigations: the

merger between two specialist retailers of gaming products, GAME and Gamestation, and the merger between two specialist book chains, Waterstone's and Ottakar's. The study assessed the consistency between the CC's conclusions on the likely future market developments and the actual market outcome. Lear found that the CC had taken the appropriate action when it cleared the mergers; price competition following the mergers had increased in both markets and the mergers had not led to any substantial lessening of competition in either market.

3.3 *CC Market Investigations*

69. Under the Enterprise Act 2002 (section 131), the OFT has the power to refer a market to the CC for further investigations where it has reasonable grounds for suspecting that any feature, or combination of features, of a market in the UK for goods or services prevents, restricts or distorts competition in connection with the supply or acquisition of goods or services in the UK or part of the UK. It is for the CC to decide if this is the case and, if so, whether action should be taken.

70. If it identifies adverse effects on competition (AEC), 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.

3.3.1 *Description of CC Market Investigations*

71. During 2011/12, the CC progressed five market investigations, two of which were referred during the year (supply of aggregates, cement and ready-mix concrete, and statutory audit services) and one of which was completed (local bus services).

- Local bus services

The OFT referred UK local bus services, excluding London and Northern Ireland, to the CC in January 2010.

In December 2011, the CC published its final report. The CC confirmed its provisional findings (notified in May 2011) that in many areas bus operators face little or no competition, leading to passengers facing less frequent services and, in some cases, higher fares than where there is some form of rivalry. And also that the way some local authorities tender for supported services—necessary bus services which would not be provided without public support—can also restrict competition.

The CC identified a number of factors that restrict entry and expansion into local areas by rivals and otherwise stifle competition and outlined a package of measures to tackle these factors and open markets up in future. Such measures include providing more effective multi-operator ticketing schemes, ensuring fair access to bus stations, measures addressing operator behavior, strengthening the tendering process, close scrutiny of bus mergers and encouraging 'competition-friendly' partnerships between local transport authorities and bus operators.

The CC is working on implementing remedies in this completed market investigation (<http://www.competition-commission.org.uk/our-work/local-bus-services>).

- Movies on Pay TV

In August 2010, the Office of Communications (Ofcom) referred the supply and acquisition of subscription pay TV movie rights and the wholesale supply and acquisition of packages including core premium movie channels (ie Sky's movie channels) to the CC for investigation.

In August 2011, the CC published its provisional findings, in which it found that Sky's control over pay-TV movie rights in the first pay-TV window in the UK restricted competition between pay-TV providers. Following those provisional findings, there were a number of material developments in the market and the CC reappraised its previous analysis in the light of both these developments and of the responses received to its provisional findings.

This led to the publication of revised provisional findings in May 2012 in which the CC provisionally found that Sky Movies no longer provided Sky with a material advantage over its rivals in the pay-TV retail market. Whereas in the past, consumers wanting to watch recent movies on a pay-TV movie service had to subscribe to Sky Movies through a traditional pay-TV platform, the launch of new and improved movie services in the pay-TV market meant that other alternatives were now available. The CC expected consumer choice to increase further when Sky launched its own Internet-based service in the summer which would offer Sky Movies without the need to take any other pay-TV content or subscribe to Sky's satellite platform.

The CC is inviting comments on its revised provisional findings. The statutory deadline for the CC's report is 3 August 2012 (www.competition-commission.org.uk/our-work/movies-on-pay-tv).

- BAA airports

In March 2009 the CC published its final report on the BAA airports market investigation. This report required BAA to sell three airports including Stansted, Edinburgh or Glasgow and Gatwick (which BAA sold in December 2009). The decision was subject to a legal challenge by BAA, which eventually culminated in the Court of Appeal reinstating the CC's findings in October 2010. In February 2011, the Supreme Court refused BAA permission to appeal further.

The CC considered whether since publication of its March 2009 report there had been a material change of circumstances that should require it to reconsider the implementation of the airport sales and in July 2011 the CC concluded that the sale of the airports by BAA remained fully justified and that passengers and airlines would still benefit from greater competition with the airports under separate ownership, despite the current Government's decision to rule out new runways at any of the London airports.

BAA sold Edinburgh airport in April 2012 and the CC is working on implementing the other remedies in this completed market investigation (through the sale of Stansted airport by BAA). The CC's decision in relation to the sale of Stansted remains the subject of appeal – refer to section 3.3.2 below (www.competition-commission.org.uk/our-work/baa-airports).

- Aggregates, cement and ready-mix concrete

The issues statement was published on 8 March 2012 and the statutory reporting deadline is 17 January 2014 (www.competition-commission.org.uk/our-work/aggregates-cement-ready-mix-concrete).

- Private healthcare

The statutory reporting deadline is 3 April 2014 (www.competition-commission.org.uk/our-work/private-healthcare-market-investigation).

- Statutory audit services

The issues statement was published on 7 December 2011 and the statutory reporting deadline is 20 October 2013 (<http://www.competition-commission.org.uk/our-work/statutory-audit-services>).

3.3.2 *Judicial Review Challenges to CC Market Investigation Decisions*

- BAA Limited v CC

On 1 February 2012 the CAT gave judgment in respect of BAA's challenge to the CC's decision in a report dated 19 July 2011 that the sale by BAA of Stansted Airport was fully justified and that passengers and airlines would benefit from greater competition with the airports under separate ownership despite the current Government's decision to rule out new runways at any of the London airports. The CAT upheld the CC's 2011 decision to require BAA to sell Stansted Airport. BAA has been granted leave to appeal to the Court of Appeal.

<http://www.catribunal.org.uk/238-7271/1185-6-8-11-BAA-Limited.html>

4. **Resources of competition authorities**

4.1 *Resources overall (current numbers and change over previous year)*

72. 2011-2012 is the first year of a four-year HM Treasury funding cycle. The OFT's budgets have been set for 2011-12 to 2014-15 following the Spending Review 2010. As such, the OFT's budget will be reduced by 25% in real terms over the next four years of the funding cycle.

4.1.1 *Annual budget (in your currency and USD):²*

73. At the OFT there is no formal split between the OFT's competition and consumer work, so there is no 'competition-related budget' as such. However, following an analysis of work carried out by relevant parts of the organisation, the OFT estimates the breakdown of the total settlements from HM Treasury for competition work for 2011-2012 as being £11 million (approximately US\$17.3m). This excludes market studies work.

74. The CC's budget for 2011-12 was £17.8 million (approximately US\$27.9 million) and its budget for 2012-13 is £17.1 million (approximately US\$ 26.8 million) a reduction of 3.9% to its 2011/12 budget. All the CC's budget is competition related.

4.1.2 *Number of employees (person-years)*

75. The OFT estimates that its externally facing competition interventions (including casework, policy and advocacy, as well as strategic and other support functions) account for approximately 115.7 staff (full-time equivalent). This does not include staff involved in general markets work, which has competition and consumer dimensions.

76. Approximately 108 of the OFT's staff working on competition enforcement have non-administrative roles, of which 39 are economists and 38 are lawyers. The OFT's Mergers team consists of 20 non-administrative staff.

77. The CC has 132 employees, approximately 71 of whom work on competition enforcement and have non-administrative roles – 15 are lawyers, 28 are economists and 28 are either financial and business advisers or other inquiry staff.

4.3 *Period covered by the above information*

- April 2011 – April 2012

² Assuming an exchange rate of GB £1 = US \$1.5735.