

UK MERGER CONTROL PROCEDURE THE COMPETITION COMMISSION PERSPECTIVE

Talk by Peter Freeman¹ to the
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Introduction

...(I)f the matter goes to the (Competition) Commission, there is a good deal more transparency and depth in the decision-making process than is the case at the stage of the OFT. The Commission seeks comments from, and holds hearing with, all interested parties. Facts can be investigated in depth. The issues letter is published for all to see. The final report contains a summary of the evidence received, who gave that evidence and the Commission's own detailed analysis. Everybody knows who said what.

Surprisingly enough those comments were not made by the Competition Commission (CC) itself but by the Competition Appeal Tribunal (CAT) in its first Enterprise Act judgment in the *Hospital Software* case.² They paint a fairly rosy picture, which will be recognizable to at least some of those present today. My purpose in this talk is briefly to examine the CC's processes to see whether they measure up, on paper and in practice, to the plaudits bestowed by the CAT. Needless to say, these are my personal views, not necessarily those of the CC.

I propose to look at what the CC aims to achieve by its procedures; to see what issues have arisen in recent cases; to identify issues that are ongoing and possibly unresolved; and to look briefly at the significance of the judicial review process, which underlies and in a sense underpins the CC's procedures, if not all of its activities.

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²*IBA Health Limited v OFT supported by Isoft and Torex*, [2003] cat 27 at paragraph 206.

The objectives of CC procedures

The CC's procedures are not helpfully set out in a single place but are to be found in statute,³ in the CC's own Rules of Procedure,⁴ which the CC's Chairman is required to publish, and in other guidelines published by the CC,⁵ all supplemented and refined by experience and practice. The CC has a large discretion to determine its own procedure but is now required to publish its rules, after appropriate consultation.

The purpose of these procedures is to provide the necessary framework for the performance of the CC's general functions. These functions are to conduct inquiries into markets, mergers and regulatory issues, all on reference from other bodies.⁶ The CC is required to investigate complex issues in depth within tight statutory time limits and to do this it must gather and assess evidence both written and oral. The CC is further required to come to reasoned decisions on matters which are liable to affect the rights and obligations of parties involved in the investigation and therefore must observe due process in putting matters to the parties and giving opportunity for response. At the same time it must have appropriate regard to confidentiality, which places limitations on the free exchange of evidence and argument between parties involved in any investigation. Finally the CC is required to frame remedies to address in as comprehensive a way as possible any adverse findings that it makes.

These are challenging duties and establishing a set of procedures that allows successful discharge of all of them is no easy task. The three objectives of speed, fairness and thoroughness can give rise to conflicting incentives but I suggest this is a matter of equality not hierarchy and none can be sacrificed to the others.

³Competition Act 1998 Schedule 7 as amended by the Enterprise Act 2002 s187, especially paragraphs 19 and 19A.

⁴CC1 June 2003.

⁵In particular, Chairman's Guidance to Groups (CC6), Chairman's Guidance on Disclosure of Information (CC7) and General Advice and Information (CC4).

⁶This paper concentrates on procedure in merger cases as no market inquiry has yet been completed under the Enterprise Act and regulatory inquiries are *sui generis*; however the 'read-across' from mergers is substantial.

The conduct of inquiries

So how does the CC conduct an inquiry? The first point is that the CC operates through groups.⁷ Once a group and its chairman have been selected by the Chairman, the conduct of an inquiry is in the hands of that group. It must of course observe statute and the CC's rules of procedure, and take account of any relevant guidance, but may otherwise determine its own procedure. The CC makes strenuous efforts to ensure procedural consistency between inquiry groups and has a permanent group (the Remedies Standing Group) whose task is to assess and decide on remedies (including procedural aspects) when no inquiry group is empowered. The CC's staff, of course, work with and support each group which helps to ensure consistency. But, strictly speaking, each inquiry group not only represents the CC, but in a real sense *is* the CC for the purpose of its procedures.

In essence an inquiry falls into five stages; not always separate but mostly sequential:

1. Initial fact finding.
2. Identification of issues.
3. Provisional findings and possible remedies.
4. Final decision.
5. Detailed implementation of remedies (if applicable).

Fact-finding

This is carried out by asking for evidence, sending questionnaires, visiting the parties' facilities and holding meetings with staff and formal hearings. The CC may conduct or commission surveys or economic or other assessments. The parties to the merger will be closely involved in most of these matters, particularly the visits and questionnaires. They are normally consulted on the nature and specification of surveys. Non-confidential versions of evidence are requested from parties and these go on the CC's web site. Some parties may

⁷CA 98 Section 7, paragraph 15.

say they were not sufficiently consulted, or their points not fully taken. The problem is that someone has to drive the case forward and, like prayers, not every point made can necessarily be accepted. All, however, are carefully considered. Other factual material is also published, including survey reports, and summaries of third party evidence received.

Identification of issues

This is done in the eponymous Issues Letter, also announced to the public. Issues Letters have been criticized for being both too bland and too comprehensive and these criticisms have been noted. Issues letters may become considerably more focused, or even discarded altogether as adding nothing to the parties' understanding. At present, they serve to set a maximum scope to the matters under investigation, however, and are the culmination of a process of assessment that goes hand in hand with the fact-finding process. So far as the main parties are concerned, it is now CC practice to share quite detailed Working Papers with them, which set out the investigation team's current thinking (other than opinions, conclusions or legal advice) and which flesh out what lies behind the rather formal Issues Letter.⁸ This means that the provisional findings should not come as a surprise to the merger parties.

Provisional findings

The publication of provisional findings, coupled with a notice of remedies (if applicable) is an innovation in procedure. These are the culmination of a process of putting issues to the parties and obtaining their response and are in no sense an 'opening bid' by the CC. They do play an important part in the consultation process on the substantive finding but they also enable a rational discussion of possible remedies. So far the procedure has worked well in the three mergers that have gone to the remedies stage, *Stena*, *ScotRail* and *Dräger*.

⁸See CC 7, paragraph 3.5(h).

There have been issues over confidentiality. Parties have sought to excise large sections of the provisional findings. Time has had to be allocated to deal with this aspect. The CC is required⁹ to publish its findings and its reasons and wholesale excisions can make a nonsense of this. Excision of the whole of our party's arguments, for example, could make the CC's decision incomprehensible.

Provisional findings were conceived to facilitate the process of making an adverse finding, to make the identification of possible remedies more rational and to give the affected parties a proper opportunity to respond to the CC's views before a final decision is made.¹⁰ Where the finding is not adverse, third parties have used the provisional findings to put their own views. It is fair to say that whilst third parties see the main parties' published contentions, they may see less of the CC's emerging views. In particular they will see in advance of the provisional findings only those parts they need to see for excision purposes. So the provisional findings have proved to serve an additional less clearly foreseen purpose in this respect.

Notification of remedies

It was a common complaint under the Fair Trading Act regime that the CC's discussion of remedies was too academic and contingent. Combined with the fact that the CC now itself decides on and implements remedies, discussion of them in draft, as it were, must be seen as a helpful step. Parties may not like the medicine, but they can have a say over what form it should take. Again experience to date has been positive and the CC takes this aspect of its new functions extremely seriously.¹¹ In *Dräger* and in *ScotRail*, the behavioural undertakings that emerged were extremely detailed and resulted from a process of close consultation with the parties concerned and from third party comments.

⁹See CC Rules of Procedure, § 10.4 and 10.8.

¹⁰Enterprise Act §104(2) and 169(2) impose duties on the CC to consult.

¹¹See the CC's recent draft guidance on divestiture remedies in merger inquiries.

Final decision

Although the statute refers to reports¹² the CC in effect takes decisions. There have been valiant, and for the most part successful, efforts to make these concise, clearly readable and understandable. The evidence on which they are based appears in appendices (often more extensively excised, alas) and in the CC's published inquiry materials. The aim is to have a reasoned decision that is understandable to the public as well as to the parties and which will, it is hoped, contribute to the established body of CC practice (I hesitate to call it case law). We are giving active consideration to the scope and number of the appendices attached to our decisions.

Implementation of remedies

This stage should be distinguished from the identification of and decision on remedies. It involves a process of discussion with the affected parties and a wider statutory consultation procedure¹³ resulting in the acceptance of signed undertakings or, in theory, the making of an order. In *ScotRail*, the process is still under way.

Recent cases

Let us now look at the experience of the new system. The CC has dealt with the following cases under the Enterprise Act.

Stena and P&O

This case was referred to the CC on 22 August 2003, provisional findings were published in summary on 28 November 2003 (and in full a week later) and the final report published on 6 February 2004. It concerned a proposed asset acquisition by Stena of ferry operations on the Irish Sea between Liverpool and Dublin and Fleetwood and Larne. The closure of P&O's Mostyn–Dublin route was contemporaneous. The inquiry focused on freight and concluded

¹²Enterprise Act s39.

¹³Enterprise Act, Schedule 10.

that there would be a significant lessening of competition (SLC) on the southern route but not on the northern route. The CC consulted on two possible remedies either prohibiting the southern route transfer or promoting greater access to Dublin berths. Stena proposed behavioural undertakings to mitigate the effect of its stronger market position on the Dublin routes. After examining the likely effectiveness of the behavioural options, the CC concluded that only prohibition of the southern route merger would be sufficient to remedy the SLC identified and this was accepted by Stena; a notice of proposal to accept undertakings was issued for consultation on 7 April 2004 and, with insignificant amendments, undertakings were accepted, signed and published on 15 May 2004. The southern route merger was also subject to control by the Irish Competition Authority, whose procedure did not proceed to final determination as a result of Stena's acceptance of the CC's proposed remedy.

Dräger Medical and Hillenbrand Industries

This case was referred on 18 December 2003, provisional findings were published on 5 March 2004 and the final report published on 19 May 2004. It concerned the acquisition by Dräger of the Air-Shields business of Hill-Rom, a Hillenbrand subsidiary. The business was the supply of neonatal warming therapy products to UK hospitals for use in labour and delivery wards and in neonatal intensive care units. Both groups sold these products in the UK through distributors and had no production facilities here. The merger was not primarily directed at the UK and, as may be expected, there was in the UK a single customer, the NHS, albeit taking various forms for procurement purposes. The CC found an SLC in three out of four product areas and went through a detailed process of remedy formulation, intended to arouse the latent buyer power of the NHS and to control the behaviour of the merged group in the interim. The case is significant in that the remedies involved recommendations to UK health departments and agencies and the feasibility of these recommendations had to be explored in detail before the report was finalized.

Carl Zeiss and Bio-Rad

This case was referred on 30 December 2003, provisional findings were published on 19 March 2004 and the final report was published on 17 May 2004. This was an acquisition of the worldwide microscopy business of Bio-Rad Inc by the German group Carl Zeiss. The products concerned were advanced 3D optical microscope systems, particularly those using multiphoton techniques. These were expensive items (up to £500,000) and the market was characterized by innovation and product differentiation. Bio-Rad's assembly facilities were located in the UK. On a comparison of the effects of the merger with the likely counterfactual, the CC found no SLC, with the position in relation to multiphoton microscopes heavily circumscribed by patents owned by Cornell University and exclusively licensed to Bio-Rad. The CC noted certain assurances given by Carl Zeiss as to their future intentions should the merger be allowed to proceed.

FirstGroup and the Scottish Passenger Rail Franchise

This case was referred in 13 January 2004; provisional findings were published on 28/30 April 2004 and the final report was published on 28 June 2004. The remedies stage, still in progress, is expected to complete in October before the SRA awards the franchise on 17 October 2004. It concerned the proposed acquisition of the ScotRail franchise by FirstGroup. The CC examined issues of overlap between bus and rail transport in Scotland, particularly Glasgow and Edinburgh. It found an SLC in relation to various bus/rail route overlaps, and more widely in relation to public transport networks in Strathclyde, Edinburgh and elsewhere in Scotland. FirstGroup was confirmed as the preferred bidder in the SRA franchise award process on 11 June 2004. The CC concluded that the SLC could be addressed by behavioural undertakings and, following the publication of the report, a detailed process of articulating, negotiating and agreeing the required remedies has been underway. As the case is not complete, I do not wish to comment further.

Several other proposed mergers were abandoned¹⁴ and there are no less than eight merger cases currently in progress.¹⁵

Lessons from the cases

Whilst not perhaps on the scale of *GEC/Honeywell* or *Microsoft*, these cases nonetheless offer some useful guidance on process—which may be of more general application. I want to consider the three areas—speed, fairness and thoroughness.

Speed

It is a common complaint that merger control takes too long. In my view, the CC's handling of cases under the Enterprise Act has been quick enough to pass criticism on this count. In *Stena*, the total time taken was 24 weeks, in *Dräger* 22 weeks, *Carl Zeiss* 20 weeks, *First Group* 24 weeks. These are, obviously, in EC parlance, Phase II cases and the total time taken stands comparison not only with ECMR phase II practice, but also with previous UK Fair Trading Act practice. But there are two important caveats. First, the introduction of provisional findings means that the likely view on the merits of the merger is known normally within 14 weeks of the start.¹⁶ Second, and related to this, the CC's 24-week process now includes the decision on remedies (although detailed implementation of remedies is in addition to this) and what is published is the final redacted version. In comparing the new system with the Fair Trading Act, like must be compared with like, so that the comparison is with the time previously taken from the reference to the Secretary of State's announcement

¹⁴*WBB/Tarmac Central* (silica), *Unum/Swiss Life* (financial services), *AAH/East Anglian* (pharmaceuticals), *Convatec/Acordis* (speciality fibres), *National Milk Records/Cattle* (animal information services).

¹⁵*Archant and INM* (London local newspapers), referred on 29 April; provisional findings issued on 29 July 2004.

DS Smith/Linpac Containers (corrugated case materials), referred on 20 May; provisional findings published 8 September 2004.

NEG/Greater Anglia (bus/rail), referred on 27 May 2004.

Knauf Insulation/Superglass Insulation (glass fibre), referred on 17 June 2004.

Emap/ABI Building Data (specialist data supply), referred on 1 July 2004.

Taminco/Air Products (chemicals), referred on 16 July 2004.

Arriva/Sovereign (buses), referred on 3 August 2004.

Arcelor/Corus (hot steel pilings), referred on 10 September 2004.

¹⁶The times to provisional findings were, respectively, *Stena/P&O* 14 weeks, *Dräger* 11.5 and weeks, *Carl Zeiss* 11.5 weeks and *FirstGroup* 15 weeks.

of her decision, frequently adding six weeks to the three or four months of the CC's work.¹⁷ On that basis an average of 22 weeks is good.

Can we speed the process up for 'single' or 'small' cases? It would be nice to think so. In *Dräger* and in *Carl Zeiss* the time to provisional findings was 11.5 weeks, but, even so, 'small' cases can generate complex issues which require careful analysis. Given the time needed to gather facts, conduct surveys and hear the parties, what risks being squeezed out is the time for assessment and deliberation, which is hardly desirable. Nevertheless, this remains an area of concern to the CC.

Fairness

Has the CC been fair in its proceedings? I believe the answer is very clearly positive. The CC offers the merging parties continuous and increasing access not only to the evidence emerging during the inquiry but also, and much more importantly, to its thinking, culminating in provisional findings. Of course there are issues and difficulties with this and no one claims perfection, as yet, but the CC compares very well with other authorities in this respect. The following points arise:

Confidentiality

Much as we might like to, it is usually not possible to pass one party's evidence unaltered to all the others for comment. Customers, suppliers or competitors may wish to keep anonymity, in some cases for fear of retaliation or to excise part of their evidence; failure to meet these concerns may limit their willingness to provide evidence at all. A method of putting a sufficient amount of such evidence to the relevant parties has to be operated. We start by requesting the provision of non-confidential written evidence, with a view also to placing this on our web site. We also summarize the bulk of third party evidence and put

¹⁷Of the Fair Trading Act cases decided in 2003 the shortest was *Arla/Express Dairies* at 14.5 weeks and the longest *Carlton/Granada* at 30 weeks. The *Arla* case was subject to a deadline under Article 9 ECFR.

that summary to the parties. Larger, more specific, submissions may be put as they stand, with as few excisions as possible. And confidentiality will inhibit too much 'drilling down' into individual survey responses, although surveys, methodology and reports are generally made freely available.

Working papers

These are developed by the CC inquiry team to inform thinking as the inquiry develops. Drafts and final versions of most working papers (excluding opinion, conclusions or legal advice) will normally be shared with the parties for comment. General factual papers will normally be put on the web site; this is more difficult with analytical papers as they may rely on confidential data from the parties or elsewhere. They may, however, mutate into appendices to the provisional findings.

Hearings

These are the CC's unique feature; a lot of work goes into hearings, on all sides, but they do allow the CC panel to engage directly with senior management of the merging parties and others and vice versa. They are not intended primarily to be a forum for obtaining factual information, but rather to air views, test arguments and provide the opportunity to 'be heard'. They are regarded by the CC as an extremely important part of the inquiry process and we seek to improve them in any way possible.

Thoroughness

I do not need, or want, to say much on this. The CC conducts thorough investigations and is not normally criticized for cutting corners. However, the time constraints necessarily limit what is possible in a merger inquiry, in comparison for example, with a market investigation. Thus there is generally time for one round of survey work only—and quantitative and qualitative aspects will normally be elided. A merger inquiry is a project, and there is a great

premium on project management, particularly in the early stages. Well prepared and cooperative main parties can assist materially in this process.

Ongoing issues

Finally, let us consider some issues that are still unresolved, or where the practice is still evolving. I would mention the following:

Cancellation of references

In several cases¹⁸ the parties have either cancelled their arrangements following a reference or restructured them to avoid the issues identified in the reference. In some instances there may be grounds for thinking the object of the proposal has been achieved even if the proposal itself has been abandoned. There are three points to note here.

First, the FTA provision¹⁹ under which the closure of a business by agreement qualified as a merger has been dropped from the Enterprise Act. The scope of merger control has therefore been narrowed.²⁰

Second, the OFT is well aware of the risks associated with too narrow or too specific terms of reference. Whilst the issues causing the OFT to make the reference need to be clearly identified, the CC needs to be able to consider any given transaction and the issues arising in the round.

Third, under the Enterprise Act, if the referred arrangements have actually been abandoned, the CC has a duty to cancel the reference,²¹ and it may then be difficult to impose conditions or obtain assurances that the same proposal will not be repeated or its objectives attained in

¹⁸See footnote 10.

¹⁹FTA s65(1)(6).

²⁰So, the closure of the Mostyn–Dublin route in *Stena* was considered as part of the background to the merger rather than as a merger situation in itself.

²¹Enterprise Act s37(1).

some other way, although there will generally be the possibility of a further reference by the OFT.

Third parties

Much of the focus of the new rules of procedure is on the position of the merging parties referred to in our rules as 'main parties'. They are required to have the provisional findings notified to them²² and it is assumed that they are the parties likely to be adversely affected. However, in cases where no SLC is found, it may be a third party whose interests are affected. Thus in *Carl Zeiss*, the main competitor, Leica, objected strongly to the proposed clearance. As a result, Leica made written comments on the provisional findings and attended an oral hearing; the main parties, not surprisingly did not do so; the CC's rules may need to say more about the position of third parties in such a situation, possibly by giving them a specific entitlement to be notified of the provisional findings.

Transparency

I have described how the CC's makes its process as transparent as it reasonably can. There remains the objection that the CC does not grant 'access to the file' in the sense understood in the ECMR or CA 98 context. This is not a closed issue, but the CC would need to be convinced that any alteration in its practice in this respect fulfilled a real, rather than a formalistic need. Unlike those of the EC Commission, CC merger procedures are not to any significant real extent 'pre-loaded' and the inquiry starts when the reference arrives. The CC will therefore tend to look more favourably at transparency improvements which do not hold up the inquiry. At the start of the inquiry, there will be no 'file' to inspect so the parallel with the ECMR and with competition cases is not strictly valid anyway. It would be better to focus on whether parties have sufficient access the CC's evidence and views, as

²²CC Rules of Procedure, s10.3. Rule 10.8 also requires that they be published.

they emerge during the inquiry, and on which, under present procedures, the CC is quite generous. So I suspect this issue is a red herring.

The counterfactual

Whilst not strictly a procedure point, the CC's stress on a fair assessment of the likely counterfactual (the situation with which the merger's effects should be compared) may be noted. Whilst the starting point is the pre-merger situation, the CC will consider and assess likely alternatives. This can decide the result. Thus in *Carl Zeiss*, where one of the leading optical microscope companies acquired another, the counterfactual was not the pre-merger situation but the acquisition of the target company by one of the other competitors. The analysis therefore was between the merits of alternative acquisitions with no overall reduction in competition resulting from the merger. The CC will, however, test counterfactual claims very carefully before forming any expectation.

Interim measures

Practice is developing in this area, both with the OFT and the CC, and it is necessary to distinguish between anticipated and completed mergers. The statute provides that for anticipated mergers, a reference results in an automatic restriction on further share dealings,²³ but not in relation,²⁴ to assets. For completed mergers,²⁴ the statute prevents the completion of outstanding matters in connexion with the merger without the CC's consent. The situation the CC addresses will therefore vary according to the stage the merger has reached and what the OFT has done.²⁵ In two recent and current cases of completed mergers (*Archant* and *DS Smith*) the CC sought undertakings, in addition to the statutory restrictions, so as to preserve so far as possible the viability of the acquired business should the outcome of the inquiry be adverse to the merger. In another case (*Emap*), the CC

²³Enterprise Act s78.

²⁴Enterprise Act s77(2).

²⁵Note that the Cc may, if the facts justify it, treat a completed merger as an anticipated merger, and vice versa (Enterprise Act s37(2)).

adopted initial undertakings accepted by the OFT and subsequently sought variations to them, for a similar purpose.

Judicial review

This remains rather like the ‘elephant in the corner’—it is sitting there but no one mentions it, largely because it hasn’t happened yet: but it surely will, and in the one case that has happened involving the OFT with which I introduced this talk, there were plenty of references to the CC and its processes. The following points occur:

First, as already mentioned, the CAT referred to CC process with approval, but this is in the abstract. The CAT has as yet considered no specific CC case and whilst we are confident, we are not complacent. The CC strives to act legally, rationally and fairly and will defend its position in front of the CAT as necessary. It will not regard a case going to judicial review as surprising, or as an affront. The establishment of a specialist tribunal, able to review the activities of the competition authorities, is seen as an appropriate and beneficial safeguard to the inquiry process and not as something to be feared.

But there is a paradox in this, at least in respect of review on grounds of procedural fairness. The CC’s procedures now involve so much interface with the parties that it is much less likely that things will come as a surprise, or an opportunity to comment will be denied. The Enterprise Act has made applying for judicial review easier, but it may have made it potentially less rewarding. Time will tell.

In conclusion

The past year has produced no insuperable procedural problems. There are several important ongoing issues, and the CC will continue to review and amend its procedures as its experience of the Enterprise Act grows. As yet, its new processes have not been formally

questioned before the CAT, or any other Court. As an interim report, therefore, the verdict is 'satisfactory progress, but the pupil's abilities have yet to be fully tested'.

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