

**THE THIRD ANNUAL COMPETITION COMMISSION, COMPETITION TRIBUNAL
AND MANDELA INSTITUTE CONFERENCE ON COMPETITION LAW,
ECONOMICS AND POLICY IN SOUTH AFRICA**

**The effectiveness of competition authorities: prioritization, market inquiries
and impact**

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Who we are and what we do

It is a great pleasure to be here among so many friends and colleagues and to pay tribute to the tremendous work already done and being done by the competition authorities in South Africa.

The UK and South Africa have many things in common, including a Competition Commission, but the nomenclature can be confusing, as the equivalent of your Competition Commission is not our Competition Commission, but rather our Office of Fair Trading; and our Competition Commission bears some resemblance to your Competition Tribunal whilst our Competition Appeal Tribunal is more like your Competition Appeal Court. Indeed, so confusing can this be that for a while, my daily press pack of competition reports included by mistake quite a number of clippings about the activities of the South African Competition Commission, attributing their achievements to us—many thanks!

Whatever the names we use, the issues we face are very similar. I hope I can explain a little about what we do in the UK in relation to prioritization, in market inquiries and in evaluating the impact of our measures.

The CC

The Competition Commission (CC) is one of two UK competition authorities (the other being the Office of Fair Trading (OFT), represented here today by John Fingleton). We are both independent from the executive arm of government.

The CC and its predecessors in various disguises can be traced back 60 years now, but we have only operated in our current form as a decision-making authority since 2003. Our remit is focused on mergers and markets and we also have a big role in utility regulation. In contrast to many other competition authorities, we do not apply or enforce the 'classic' competition law prohibitions against restrictive practices and abuse of market power. We do not select our own cases and we only act on references from other bodies, that is the OFT, sectoral regulators and the Secretary of State (in exceptional cases). Our task is to look at a relatively small number of cases in-depth. Our decisions are subject to judicial review by a specialist tribunal, the Competition Appeal Tribunal (CAT), but, in general, are not subject to any Ministerial control—at least not on questions of competition.

Prioritization

As we do not select our own cases, one could say that prioritization in the strict sense of the word is not an issue for us. If a case is referred to us, we are required to deal with it and cannot stop an inquiry just because on closer consideration we don't think that it justifies the effort. Most cases we see have already been looked at to some degree by another authority, so it is likely there will be some issues to consider.

But, within those limitations, obviously we exercise control over what we do and how we do it. Once we have started the analysis on a case, we have to make various choices. Which specific aspects should we concentrate on? What theories of harm are relevant? How do we test them? What evidence do we collect and how do we weigh it? What is the overall policy context and does our statutory framework allow us to 'flex' the analysis if we believe that is needed?

And there are organizational aspects to consider. How much resource do we put into policy work and into competition advocacy as opposed to casework? And in times of economic downturn, how can we ensure that we are flexible enough to further improve the efficiency and effectiveness of our cases, while minimizing any burden on businesses? These are all important questions we face and, naturally, the balance can be expected to shift over time.

Market investigations

Let me now turn to market investigations. One thing South Africa and the UK have in common is the ability to undertake market inquiries. We followed with interest the progress of the Banking Enquiry Panel here. But the UK regime, although similar, has an extra unique feature. This is the combination, in a single body, of the power to investigate, decide and apply remedies.

Part of competition enforcement

UK market investigations are in this sense to be seen as part of competition enforcement. They are not just a way of 'finding out what is going on'. Nor are they intended primarily to unearth illegal activity or punishable breaches of the law—although they may do so along the way. Instead they are meant to be a means of improving competition in a market when this is seen to be not working well.

For this purpose, we are required to identify features of the market that 'prevent, restrict or distort competition'. (That language echoes Article 81 of the EC Treaty but is actually derived from 'complex monopoly' provisions of the Fair Trading Act 1973, which preceded the current Enterprise Act 2002.) The legal test we apply is called the 'AEC' test, ie whether or not there is an 'adverse effect on competition' in the relevant market. We assess the nature and extent of rivalry between firms operating in the markets, considering the market structure, conduct of suppliers or acquirers and conduct of customers.

These investigations are detailed, thorough and robust. In the *Groceries* investigation, completed in 2008, we received over 700 submissions, held over 80 hearings in all parts of the UK, visited the parties' facilities and sites and compiled a database of over 14,000 stores covering 30 variables. The scale is comparable to your Banking Enquiry and it also took two years to complete.

What comes out of a market investigation is a detailed report with reasons and evidence, a decision on what is wrong, and detailed remedies. There is no finding of illegality or other punishments. But of course, the effects of the remedies we apply can be significant.

Pattern of cases

Since 2003 we have conducted nine market investigations. Four of these—*Store Credit Cards*, *Home (doorstep) credit*, *Personal Banking in Northern Ireland* and *Payment Protection Insurance (PPI)*—have been in the financial sector. Two have concerned transport (the *Leasing of Railway Rolling Stock* and *BAA Airports*), one in energy (*Bulk Supply of Domestic LPG*), one in information (*Classified Directories or Yellow Pages*) and one into *Grocery Retailing*.

There is no particular pattern to these cases—the market size ranges from £120 million (1.5 billion ZAR) in LPG to over £120 billion (1.5 trillion ZAR) in Groceries and some of the issues referred were quite specific—PPI rather than consumer credit as a whole, rolling stock leasing rather than the railway industry as a whole—only in *Groceries* do you get the flavour of a broader sector inquiry.

Cases we have not had

And it is also interesting to consider markets that have *not* been referred to us, despite some pressure to do so. Examples include *retail telecommunications* (where BT gave undertakings to Ofcom to head off a reference) or *retail energy* (where Ofgem preferred to carry out its own ‘probe’) or *newspaper distribution* and *credit cards*, both dealt with by the OFT under the prohibition of restrictive agreements regime—all for perfectly understandable reasons. So the use of market investigations is not particularly consistent, which may in turn tell us something about other authorities’ prioritization.

What do we look for?

So what are the factors relevant in assessing markets? Our Guidelines discuss in some detail what is meant by ‘features of the market’. Relevant factors include ‘traditional’ indicators of rivalry such as price and non-price competition, choice, quality and innovation. We also consider how open a particular market is to entry, expansion and exit, the countervailing power of buyers and suppliers, and the effect of any vertical integration.

Adverse features

Examples of market features we have dealt with to date include barriers to entry (*Classified Directories, Groceries*), barriers to switching (*LPG, NI Banking*), information shortfalls (*Store Cards, LPG*), ‘inefficient equilibria’ (*LPG, Home Credit*) and monopoly (*BAA Airports, PPI*).

In some markets we simply found *very little rivalry*. For example, *LPG* providers to domestic users generally saw themselves as having captive customers for life once the tank was installed. Similarly in *Home Credit*, customers did not shop around and providers made little or no attempt to gain customers from other companies.

Barriers to entry can include government policies that pursue other objectives but which create obstacles. In *Groceries* we found that the planning laws have an important social purpose but almost inevitably restrict competition.

Lack of information available to customers can mean that they get a worse deal than otherwise. For example, personal current account holders in *Northern Ireland Personal Banking* did not know how they could switch and the banks did little to encourage any switching.

Sometimes there are situations where the market arrives at a ‘*bad*’ equilibrium from which no individual firm has an incentive unilaterally to deviate and this often involves non-collusive oligopoly. *Home Credit* and *Bulk Domestic LPG* are good examples of this.

Then there is *monopoly*. This was a feature of the *BAA Airports* case, which is currently under appeal, while ‘point-of-sale’ monopoly was a feature of *PPI* (also under appeal).

Not enough competition

Although the CC will set out its findings using the statutory framework, a lot of this boils down to saying that, compared with what we would expect to see in a well-functioning

market, there simply isn't enough competition and consumers are getting a worse offering than they should be getting. So the question that is fairly asked is can we do anything about it? How do you make competitors compete—or compete more vigorously? How do you make a market work better? And here the remedy powers of the CC take us straight into the potentially hazardous territory of market intervention. We are not just forbidding bad behaviour in the past, whether it is collusion or abuse. We are trying to change the conditions in the market to improve competition for the future.

Remedies

Turning to remedies, the statute provides that we have a duty to consider appropriate remedies and that in doing so we should have regard to the need to remedy the adverse effects 'as comprehensively as is reasonable and practicable'.

We have extensive, but not unlimited, powers of our own. But we can also recommend action by others, particularly government. These powers to make recommendations were used in *The supply of groceries in the UK market investigation* (recommending the introduction of a competition test as part of the planning system and the establishment of an 'ombudsman' to oversee the new Groceries Supply Code of Practice); and in the *Rolling Stock Leasing* inquiry to change the system of franchising train operators to enable competition in rolling stock acquisition to work better.

Recommendations can be important but the key aspect of our remedy powers is our power to intervene directly on the market. This can, exceptionally, involve setting prices (as it did in *Classified Directories*—although with a sunset provision). More importantly, it can mean ordering the divestment of assets or the break-up of companies.

This is a very significant power, and possibly an unusual one to entrust to an agency in circumstances where no illegality has to be found. So far the only case where we have felt obliged to apply divestment is the *BAA Airports* case, where we had to consider the position of the privatized former state-owned airport operator. We found that competition would improve if BAA's three London airports were separately owned, and similarly with its two Scottish airports. BAA has appealed that decision and the case continues.

In summary, UK market investigations are unique internationally because they are not only thorough and legally structured investigations but also contain a direct remedy power. The fact that certain aspects—mainly specific remedies—of three of our market investigations (*Groceries*, *PPI* and *BAA Airports*) have been the subject of appeal to the CAT shows first the seriousness and potential impact of what we are doing, and second the robust legal framework in which we operate and the Government's concern to avoid the application of these major powers being seen as arbitrary or not subject to proper control. We are quite content to operate within these constraints.

Impact

Let me turn now to consider briefly how we assess whether we are delivering value for money. Demonstrating benefits from activity is essential for any competition agency that is properly accountable.

We consider it important to measure and evaluate the impact of what we do, not only to improve and refine how we work but also as part of our accountability to the general tax-paying public. Here we have to take account of the fact that we are part of a larger system and work jointly with other authorities.

Detriment and benefit

In our current Annual Report, we estimated that the value to the consumer of the CC's and the OFT's joint activities in relation to mergers and markets work in the current year was just over £600 million (7.5 billion ZAR). We have a formula for allocating benefits between the individual authorities, we estimate that the figure attributable to the CC in 2008/09 to be just over £400 million (5 billion ZAR). This is against our costs of £21 million (265 million ZAR).

Outcomes

As well as calculating the value of the consumer detriment we have addressed, we have also evaluated our work by looking at the outcomes and processes of past cases. Working on our own or jointly with the OFT and other bodies, we have commissioned or ourselves carried out several significant *ex-post* evaluations of our mergers work (PWC 2005, Deloitte 2009), of our work overall—ie mergers, markets and regulatory (CC in-house 2008)—and of our remedies (CC in-house 2008). Let me say a few words about each of these.

Mergers and regulatory

In relation to mergers, the recent 2009 Deloitte study looked at mergers at both OFT and CC stage, supplemented by merger simulation in half of the cases. As regards the CC's inquiries, the decisions included a mixture of unconditional clearances, conditional clearances and prohibitions. While there was some testing of certain aspects of the analysis, there was no suggestion in the report that the analysis was in any way 'wrong' or substantially flawed, although in two cases events turned out differently from the prediction.

In the 2005 *ex-post* evaluation of mergers, PWC assessed 10 of the 29 cases cleared by the CC in the period from 1992 to 2002, out of a total of 120 reference cases. The aim was to assess if the finding that the merger would not result in a significant lessening of competition was correct. Overall, the study concluded that effective competition had resulted in all of the cases studied, with no evidence of substantial and/or sustained competition problems. In two of these cases, short-term concerns seemed to have been resolved through new entry.

In 2008, we conducted an in-house evaluation of four past CC cases (two merger prohibitions, one merger clearance and one regulatory inquiry) which had been completed between January 2000 and December 2002. The aim was to find out if the CC had made sound decisions on the basis of the available information at the time; whether the underlying reasoning was clear and consistent; and if the CC had been 'right' in light of subsequent market developments. Again, the outcome of the evaluation was that the CC's decisions were basically sound and that market developments are not always predictable. But all these inquiries were carried out before the CC issued guidelines, and we found that some aspects of the decisions could have benefited from spelling out the issues more clearly and by focusing more on the economic effects of the transaction.

We have not so far evaluated the substantive findings in a market investigation. It is still too early to judge.¹

It is clear from all these reports and evaluations that, particularly in merger control, we face a challenge to the extent that markets often 'move on' in directions that cannot always be fully anticipated. Equally, this means that changed market conditions may make it difficult to

¹The OFT, however, reviewed the operation of the *Store Cards* measures, and the continued appropriateness of the remedies applied in *SME Banking*, a pre-Enterprise Act case, was formally reviewed by the CC.

'isolate' or measure the effects of our decisions on the market. But we believe that these exercises are essential and helpful tools to help us improve our work.

Remedies evaluation

In August 2008 we published an in-house, *ex-post* evaluation of merger remedies, covering a total of six cases (of which two had been decided under the current Enterprise Act). While the number of cases was too small to gain a statistically significant overview (compared with similar FTC and DG Comp studies which looked at a much larger number of cases), the study does provide an in-depth view of these remedies from the final report through the implementation process.

The study, which bears out our experience of operating the Enterprise Act merger regime, suggests that *interim* undertakings (hold-separates) are essential in the UK's voluntary notification system to maintain the possibility of an adverse finding and that a monitoring trustee and/or a hold separate manager can help reduce certain associated risks. These insights have informed the increasingly robust approach that the CC and the OFT take to interim measures, particularly for completed mergers.

We found that while *final* behavioural remedies are more complex and resource-intensive to develop, monitor and enforce than structural remedies, they can be effective in appropriate cases. However, the case studies suggest that structural remedies will generally address the competitive concerns with greater certainty.

These and other learning points have since fed into the development of our policy and practice and they have also informed the recent review and redrafting of our Remedies Guidance.²

Lessons learned

From carrying out and commissioning these evaluations, we are starting to learn some lessons as to how they should be designed to achieve the desired outcome.

First, the cases need to be sufficiently far in the past to see how the market has evolved after a particular decision was taken, but recent enough to remain relevant to the present.

Second, there are both advantages and disadvantages of commissioning external studies and reports carrying out or in-house assessments. It seems that an external evaluation has the benefit of greater independence and remoteness from the organization which may afford a clearer view on issues that warrant further consideration and potentially improvement. On the other hand, there may be benefits in being able to access knowledge within the organization to evaluate past cases as well as in the learning experience being achieved in-house. Maximizing the gains of evaluation is probably also about achieving a good balance of both internal and external evaluation, and finding effective ways of feeding the lessons learned back into the organization.

Third, much will depend on the selection of cases studied, to ensure that they represent a meaningful cross-section of different types of cases (ie for mergers clearances, prohibitions and remedies cases, and for remedy evaluation a mix of structural and behavioural measures).

²[Merger Remedies: Competition Commission Guidelines, CC8](#), November 2008.

Apart from these specific evaluations, all competition authorities are subject to various national and international peer review exercises, ratings and rankings which provide us with an important benchmark and contribute to the development of international best practices.

But we should not lose sight of the fact that these various evaluations are merely a way of helping us to improve our work. It would be unhelpful to get to a point where precisely quantifiable benefits are the main, if not sole, justification for our existence. It is not always possible to quantify benefits down to the last decimal point and we therefore need to keep in mind the general principle that effective competition benefits consumers and efficient businesses, over time, in terms of quality, choice and innovation as well as in terms of measurable price effects.

Conclusion

We are living in difficult times. It is no longer assumed that the free market and unfettered competition deliver the best answers. There are many interests and policies that challenge this position.

It is more important than ever to be able to show that competition authorities' activities are effective and valuable to consumers. We are faced with higher expectations with regard to accountability and transparency, to explain what we do, how we do it and how it benefits consumers. I believe that both effective enforcement and advocacy are indispensable in fulfilling our role effectively and this has not changed as a result of the current difficult economic climate. But we should also be aware that there may be a danger of expecting too much in terms of quantifying consumer benefits and we may, to some extent, need to manage the public's expectations. This is particularly to avoid falling into the trap of allowing ourselves to be judged exclusively in terms of short-term quantified costs and benefits, ignoring the longer-term, qualitative contribution that we make to consumer welfare and to the efficiency of the economy.

I have described who we are, what we do, how we do market investigations and how we evaluate our effectiveness. I hope I have been able to show that although we at the CC have been around a long time, the challenges we face are just the same as those facing any other authority around the world, including those here in South Africa. Our task is no different from yours, that is to keep up effective casework, done without fear or favour, and to talk up the merits of competition to anyone who will listen—and particularly to those who may prefer not to.

Thank you.