



## MERGER REMEDIES: COMPETITION COMMISSION REVISED GUIDELINES

### RESPONSE TO THE CONSULTATION

#### 1. INTRODUCTION

1.1 Ashurst LLP welcomes the opportunity to comment on the proposed revised draft of the "Merger Remedies: Competition Commission Guidelines" ("**the draft Guidelines**") published by the Competition Commission ("**CC**"). We regularly advise clients who are parties to mergers referred to the CC, or who are interested third parties or complainants in relation to merger references.

1.2 The comments set out in this paper primarily concern the detail of the draft Guidelines. As an overarching response, we strongly welcome the considerable expansion to the draft Guidelines which can only enhance transparency and a general understanding of the CC's approach and analytical framework in this context.

1.3 There are a few areas where we would welcome further expansion of the draft Guidelines:

- (a) **Procedure and timings:** there is much discussion of the analytical approach of the CC but little discussion of concrete procedure and timings. In particular, the procedure and timings for the negotiation and agreement of remedies is opaque at present. We accept that remedies can take very different forms and may take differing amounts of time to agree but it would be useful for all those involved in the process if, for example, an administrative timetable for the remedies process was drawn up and published, as it is for the main part of the CC's inquiry. The absence of a general or case-specific timetable can create a lack of transparency, particularly for third parties monitoring a case but not directly involved. For example, in the Tesco/Slough inquiry,<sup>1</sup> the final report was published in November 2007 but there has since been silence, notwithstanding that the CC's conclusions required divestment. The lack of transparency at the remedies stage is in marked contrast to the very open way in which the main inquiries are administered; and
- (b) **Impact of an appeal on the remedies process:** guidance would be useful on the situation where an appeal is lodged against the findings of the CC while remedies negotiation is still underway. For example, would negotiation of the remedies continue on the assumption that the CC's findings will stand; or would negotiation be stayed pending the outcome of the appeal; or would the approach depend on which parts of the CC's findings have been appealed? If it is not possible to give blanket guidance on the CC's likely approach in relation to appeals, then a commitment in the draft Guidelines that some form of public statement will be made on a case by case basis about the impact of an appeal on the remedies negotiations would be welcome. Again, this would enhance transparency.

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<sup>1</sup> **Tesco plc and the Co-operative Group (CWS) Limited**, Competition Commission (28 November 2007)

## 2. PART 1: INTRODUCTION AND CONTEXT

### Effectiveness

- 2.1 We note the emphasis at paragraph 1.8 (and throughout the draft Guidelines including paragraph 3.6) on the starting point for remedies being restoration of the *status quo ante*, or of the structure of competition as it would have been in the absence of the merger. We accept that this approach will inevitably be the starting point for a divestment remedy unscrambling a completed merger which the CC has decided to prohibit, and will also be the starting point in relation to an uncompleted merger which the CC prohibits and in respect of which undertakings are given to ensure the prohibition is respected. However, we note that the statutory duty of the CC in identifying remedies is to remedy, mitigate or prevent the substantial lessening of competition (or its adverse effects). Clearly, this duty can encompass a much wider range of options than simply seeking to reinstate pre-merger market conditions. We would urge the CC to be open to remedy proposals which remedy or mitigate the substantial lessening of competition without necessarily reinstating the *status quo ante*. Indeed, in certain circumstances (for example, where a partial divestment or the sale of a business owned by the purchaser would satisfactorily resolve the competition concerns), it would be disproportionate to require a return to the *status quo ante*.

### The costs of remedies and proportionality

- 2.2 As regards the CC's general comments in relation to the cost of remedies and proportionality, we acknowledge the point made in paragraph 1.10 that where a merger has been completed, the costs to the parties of any divestment remedy are of less significance to the proportionality assessment as the risk of incurring additional cost if the merger has to be unscrambled will typically have been part of the commercial analysis undertaken by the parties as to whether to complete the transaction before merger clearance was received.
- 2.3 However, we do not agree that the cost to the parties of remedies in conditional mergers should likewise be given less weight in the CC's evaluation than the cost of that remedy to third parties, the Office of Fair Trading ("**OFT**") or others. As the CC noted at the Mergers Remedies Guidance Launch Seminar on 27 May 2008, remedies such as firewalls can be very expensive for the parties to implement properly.<sup>2</sup> We do not agree that such costs should be given little weight in the proportionality assessment on the basis that they could have been avoided by not entering into the merger at all. It is correct that, if the parties consider that the costs of implementing a remedy are disproportionate to the commercial gains derived from the merger, they may well decide to abandon the transaction altogether. However, the aim of the EA 2002 is not to stifle merger activity, but to identify and deal with any competition detriments which could arise from merger activity. If the CC were to undertake its statutory role in a manner which had the effect of making a merger so expensive to implement that it would be commercially preferable for the parties to walk away, it would be applying the law in a manner that was inconsistent with the legislation. In relation to the proposal in paragraph 4.5 of the draft Guidelines that the parties might be required to appoint a third party monitor for behavioural remedies,<sup>3</sup> it would seem unfair to ignore the cost to the parties of such a requirement in the consideration of proportionality.

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<sup>2</sup> See page 23 of the transcript of the seminar, where the CC Chairman comments that 135 people were needed to implement a firewall remedy imposed in the Centrica/Dynegy case (Competition Commission, **Centrica plc and Dynegy Storage Ltd and Dynegy Onshore Processing UK Ltd** (2003)).

<sup>3</sup> See further paragraph 5.1 below.

## Relevant customer benefits

- 2.4 In considering what may constitute "relevant customer benefits", we note the CC's comments in paragraph 1.19 that, for example, a merger in the public transport infrastructure sector may enhance the value of the network to customers, but that such benefits might also have accrued from access or "through ticketing " arrangements and so cannot be said to have resulted from the merger. In relation to this point and the assessment, more generally, of whether the consumer benefits arising out of the merger are unlikely to accrue without the merger (or a similar lessening of competition) the CC's analysis must include a consideration of whether the alternative transaction structures are in fact objectively viable. Moreover, the assessment of the competitive impact of an arrangement other than the merger will necessarily be fairly high level in the absence of any concrete proposals with some commercial substance which can be reviewed. As such, we consider that in relation to the analysis of consumer benefits, the proposed merger should enjoy the benefit of any doubt. We note also that, just as the CC expresses a preference for structural as opposed to behavioural remedies, a merger is typically a more commercially acceptable and predictable way in which to generate consumer benefits than a horizontal agreement between competitors.

## Summary of remedies process

- 2.5 In relation to the description of the remedies process generally (paragraphs 1.21 to 1.28), there is no concrete indication of the time periods for the various steps which are outlined. Maximum clarity for procedural issues is always helpful and we would welcome an indication of the likely timeframe for this process. In particular, it is not entirely clear in the Enterprise Act 2002 ("**EA 2002**") whether the references to "days" in Schedule 10 are to calendar days or to working days.<sup>4</sup> An indication of the CC's interpretation of the time periods would therefore be all the more helpful – paragraph 1.26 makes reference to "a period of formal public consultation as specified in Schedule 10" but does not refer to the duration of that consultation period.
- 2.6 We would also welcome clarity on the extent of detail which the CC requires in relation to remedies proposals. For example, under the EC Merger Regulation,<sup>5</sup> the European Commission requires even the initial proposal of remedies to be in final form, signed and ready for acceptance by the Commission (even if the terms are subsequently amended and re-signed). Given the ability of the CC to negotiate the detail of the remedies after its final decision has been announced, we do not believe that the EC Merger Regulation approach would be appropriate or necessary under the UK regime, but it would be useful to have some indication of the level of detail which the CC requires.

## 3. PART 2: CHOICE OF REMEDIES

### Selection of remedies

- 3.1 We welcome the inclusion of guidance on behavioural remedies as there is no doubt that in some cases, they offer a pragmatic solution and should not be ruled out. Although the CC comments in paragraph 2.15 that structural remedies have been selected in "the great majority" of cases, we note that this has not been the case in almost 20 per cent of cases – a material minority.<sup>6</sup>

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<sup>4</sup> Unlike other provisions of the EA 2002, "days", as used in Schedule 10, is not expressly defined: compare section 32(4) and section 98(3).

<sup>5</sup> Council Regulation (EC) 139/2004 on the control of concentrations between undertakings (the EC Merger Regulation), OJ (2004) L24/1.

<sup>6</sup> Using the data in footnote 23 to the draft Guidelines which comments that structural remedies have been required in 17 out of 21 merger cases since the EA 2002 came into force, that would suggest that behavioural remedies have been accepted in 19 per cent of cases.

- 3.2 We also welcome the CC's acknowledgement in paragraph 2.19 that the fact that there is no obvious purchaser for a divestment package does not in itself render such a remedy unworkable.

### **Recommendations**

- 3.3 The issue of recommendations by the CC as part of the remedies package is discussed in paragraph 2.22 of the draft Guidelines. We note that it was originally expected (as noted in the CC's general guidelines on merger references<sup>7</sup>) that the Government would consider any CC recommendation and give a public response within 90 days of publication of the Commission's report, setting out options on which it proposed to consult, or changes that it proposed to make, in the light of the CC's report.

- 3.4 We note that the Government has responded to the recommendations made in the CC's Groceries market investigation.<sup>8</sup> However, we note also that there is no longer any reference to the Government's commitment to respond to recommendations in the draft Guidelines. A systematic policy of public responses from the appropriate Government department to CC recommendations can only strengthen the impact and credibility of CC recommendations. We would therefore welcome clarification from the Government and in the draft Guidelines as to the current policy regarding responding to CC recommendations, both in merger cases and more generally.

## **4. PART 3: DIVESTITURE AND INTELLECTUAL PROPERTY REMEDIES**

### **Package definition**

- 4.1 The CC comments in paragraph 3.8 that where the merger parties have made a divestment as part of a remedy, a "sunset clause" will typically be imposed which prohibits the merger parties from reacquiring the assets or shares sold for a period of 15 years. We consider that this period is too long, particularly in dynamic markets where the conditions of competition are continuously evolving. Indeed we consider that there should not be a standard sunset clause duration but that each case should be assessed on its merits. In most markets we would expect a duration of ten years to be sufficient although in fast-moving technology markets, or in rapidly expanding new markets, it may be that a five year sunset clause would suffice. We note, of course, that the sunset clause would be subject to variation or cancellation under the EA 2002.

### **Divestiture of an existing business or package of assets**

- 4.2 Paragraph 3.10 comments that where the business to be divested has been carved out of an existing business, the CC is likely to insist on an up-front buyer. We do not consider that such a presumption is appropriate: each case should be considered on its merits.

### **Alternative divestiture packages**

- 4.3 As a general principle, we would note that clients are typically extremely reluctant to propose "alternative divestment packages". In situations where the commercial rationale for the transaction is to acquire a particular state-of-the-art factory, or technology, the purchaser may prefer to walk away from the deal rather than have to offer the target assets as an alternative divestment package. That said, we welcome the confirmation in paragraph 3.14 that where an alternative divestment package is required to be agreed, this fact will be excised from the published version of the CC's report to avoid jeopardising the sale of the initial divestment business. There is no doubt that the commercial attractiveness of the initial package could be comprehensively destroyed if potential

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<sup>7</sup> See paragraph 4.20 of **Merger references: Competition Commission Guidelines** (June 2003) (CC2)

<sup>8</sup> **The supply of groceries in the UK: The Government response to the Competition Commission market investigation** (BERR) July 2008

purchasers know that by dragging their feet they could gain access to a "better" divestment package.

#### **Suitable purchasers - criteria**

- 4.4 Paragraph 3.15 states that divestment to the proposed purchaser should not create competition concerns. Paragraph 3.15(d) expands on this to state that divestment to the proposed purchaser should not create *potential* competition concerns. We consider that it is too much to require that the proposed purchaser does not give rise to any *potential* competition concerns. Potential competition concerns can be identified for many mergers which on further analysis prove to be unfounded. We consider that it is sufficient to require that divestment to the proposed purchaser does not give rise to (actual) competition concerns. We therefore consider that the word "potential" should be deleted from paragraph 3.15(d).
- 4.5 In relation to the comment at paragraph 3.17, we note the CC's concern that it should have given its approval to a proposed purchaser before the latter has undertaken detailed due diligence on the divestment business. However, we would suggest that this is not a matter about which the CC needs to have concerns. It is a commercial decision for the potential purchaser whether to run up the costs of due diligence without knowing whether it will be approved as a purchaser by the CC. In the (not unusual) situation where the transaction is subject to marked time pressure, it may be that the purchaser has no choice but to proceed. We would, in any case, urge the CC to act with all due speed when it is asked to approve a purchaser in this context.

#### **Continuing links and purchaser protection**

- 4.6 We welcome the CC's confirmation in paragraph 3.18 that continuing links between the merging parties and a business divested as a remedy may be necessary for a limited period. We note that to the extent that such links create competition restrictions which are not directly related and necessary to the merger, they will fall to be assessed under the Chapter I prohibition and/or Article 81 (in relation to which the CC does not have jurisdiction). The European Commission's Notice on restrictions directly related and necessary to concentrations (the "**ancillary restraints notice**")<sup>9</sup> contains guidance on the assessment of many of the typical on-going links which might be put in place following a merger and it would seem sensible to cross-refer to that guidance as being the starting point for the assessment of any such links.
- 4.7 Similarly, in paragraph 3.18, the CC comments that non-solicitation provisions may be approved to protect the purchaser for a limited period. The example is given of one year. We suggest that the CC should follow the standard guidance in the ancillary restraints notice, as the OFT does. Under the notice, such restrictions are permissible to protect goodwill for two years or for three years where knowhow is being transferred in addition to goodwill. We see no reason (absent specific facts in a particular case) for the CC to depart from this standard approach at EC and UK levels in relation to ancillary restraints.

#### **Intellectual property remedies**

- 4.8 We note the comment in paragraph 3.30 that the CC will usually prefer to divest a business including intellectual property, rather than simply divesting the intellectual property rights themselves. We note however, that the OFT considers that intellectual property rights can, on their own, constitute an "enterprise" for EA 2002 purposes where there is goodwill attached to the rights (typically in the form of a licensing revenue stream). As such, we would urge the CC to take a flexible approach to the divestment of intellectual property rights. If it is clear that selling an intellectual property right on its own will transfer goodwill to the purchaser, then it may be disproportionate to require the

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<sup>9</sup> OJ (2005) C56/24.

parties to divest anything additional in order to remedy, mitigate or prevent the substantial lessening of competition or its adverse effects. We would encourage the CC to consider each case on its facts in this respect.

## 5. **PART 4: BEHAVIOURAL REMEDIES**

### **Design, monitoring and enforcement**

5.1 The proposal in paragraph 4.5 that, in light of the resource constraints of the OFT, parties may be required to appoint third party monitors to oversee their implementation of, and adherence to, behavioural remedies is not an attractive one. Although the statutory monitoring duty of the OFT is basically being outsourced, it would presumably be the parties who were expected to bear the costs of such a measure (paragraph 5.4 of the draft Guidelines would appear to confirm this). The professional fees of a monitor over a number of years will be significant and could be highly disproportionate in the context of the remedy as a whole. The CC's general proposed approach of giving little weight to the cost to the merging parties of implementing remedies<sup>10</sup> seems particularly harsh in this context. Given the risk of a disproportionate burden, we consider that where the parties are required to self-monitor their adherence to behavioural remedies, the monitoring obligations and therefore costs should be kept to a minimum.

5.2 We note the CC's comment in paragraph 4.6 of the draft Guidelines that it has a duty to achieve as comprehensive a solution to the substantial lessening of competition as possible and so will seek to take steps to prevent post-merger behaviour or agreements which would constitute breaches of the Chapter I and/or II<sup>11</sup> prohibition or of Article 81 or 82. However, the CC cannot reasonably base its analysis on an *assumption* that such breaches will occur, or that the threat of public (or private) enforcement will fail to deter them, or that actual enforcement will not take place if an infringement does occur, which is what the draft Guidelines appear to be suggesting. Accordingly any such provisions should be kept to a minimum and should be very clear as to their scope and application.

### **Duration**

5.3 As noted at paragraph 4.1 above, we consider that the duration of a "sunset clause" should be determined by the facts of the market analysis which the CC will have undertaken. This is equally true for behavioural remedies.

### **Restraining horizontal market power**

5.4 In relation to the comments in paragraphs 4.23 to 4.27 of the draft Guidelines, we repeat the points made in paragraph 5.2 above as regards potential abuses of market power which would also constitute a breach of the Chapter II prohibition or Article 82.

### **Controlling outcomes**

5.5 We welcome the CC's acknowledgement that price remedies might be appropriate in suitable cases. We consider that flexibility is important in relation to remedies.

## 6. **PART 5: USE OF TRUSTEES AND THIRD PARTY MONITORS**

6.1 To the extent that the CC has standard terms which it expects to see in any divestment undertakings and/or trustee mandates or letters of engagement, we would welcome their publication, for example as an appendix to the Guidelines. This practice is adopted by the

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<sup>10</sup> Discussed at paragraph 2.2 above.

<sup>11</sup> We note that the draft Guidelines refer to sections 2 and 18 of the Competition Act 1998. In our experience these provisions are more instantly recognised under the terminology of "the Chapter I prohibition" and "the Chapter II prohibition", respectively.

European Commission in the context of the EC Merger Regulation and serves as a very useful starting point.

7. **APPENDIX A: INTERIM MEASURES**

7.1 In paragraph 6 of the Appendix, the CC comments that the merger parties may have significant incentives to run down or neglect the acquired business, in case it is subsequently required to be divested. This may be the situation in some cases but we believe that, in the vast majority of cases, the primary consideration will be to preserve the value of the acquired business as far as possible, with a view to maximising its resale price in order to offset the acquisition investment, should divestment be required. The CC does not appear to acknowledge this point of commercial reality, which should be seen as a significant balancing factor to the theoretical risk that the acquired business might be run down.

**ASHURST LLP**

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