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Head of Remedies
Competition Commission
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By Hand & Email

22 August 2008

Dear Mr Roberts

Merger Remedies: Competition Commission Guidelines Consultation Draft May 2008

We refer to the Competition Commission's (CC) press release of 19 May 2008 inviting comments on its Merger Remedies Guidelines Consultation Draft, May 2008 (the *Draft Guidelines*).

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General remarks

Freshfields has acted in a significant proportion of the merger inquiries recently undertaken by the CC, including: (i) Sportech plc/Vernons; (ii) Woolworths Group plc/Bertram Group Ltd; (iii) EWS Railway Holdings/Marcroft Engineering; (iv) BSKyB/ITV; and

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(v) Tesco/Co-op store acquisition in Slough. We therefore benefit from substantial experience in the practical application of the Draft Guidelines.

We welcome the CC's initiative in starting this review, and its canvassing of stakeholders prior to the Guidelines' formal adoption. Clear and accurate guidance enhances transparency and certainty for business, thereby enabling better business planning and the robustness of merger control decisions in the UK. In particular, we believe that the business community and advisors will appreciate the fact that the Draft Guidelines bring together in one document that which was previously to be found in three separate documents, namely, (i) CC2, CC8 and the guidance on interim measures.

We set out below a number of specific comments on the Draft Guidelines, on both substantive and practical issues.

The balance between effectiveness and proportionality

As before, the Draft Guidelines continue to draw inspiration from the CC's duty under the Enterprise Act 2002 (the *Act*) to "have regard to the need to achieve as comprehensive a solution as is reasonable and practicable" (emphasis added). However, in their current form, the Draft Guidelines suggest an intention to interpret this duty as if the words emphasised above had not been written in to the Act. Despite the wording of the statute, the object appears to be to achieve "nothing less than" a comprehensive solution. This approach underpins a number of key steps in the CC's analytical approach to the determination of remedies.

We believe such an interpretation runs contrary to the Act, and also risks diluting the importance of the proportionality assessment, thereby weakening an important safeguard for merging parties.

In practice, it may create a situation where the default position is to seek more in terms of a remedies package in the interests of "effectiveness", bearing in mind that the cost of the remedy to the merging parties will be attributed less significance by the CC under the Draft Guidelines (see paragraph 1.10). This outcome is not unlikely given that the Draft Guidelines state that the CC will seek to achieve a "high degree of certainty" (see paragraph 1.8(d)) that the remedy will achieve its intended effect, notwithstanding the inherent uncertainties involved in making predictive assessments of this nature. The net effect of this approach may be to deter transactions where, for example, the remedy assessment may

require a novel approach; merging parties are unlikely to want to take the risk of having to offer unnecessarily severe remedies.

Consequently, we believe that there would be merit in the CC reconsidering whether the approach taken by the Draft Guidelines should be revised.

The new remedies “universe”

The introduction of the new analytical framework in which to consider remedies is to be welcomed. We believe that this provides a useful frame of reference in which to consider remedy selection because it outlines the weight that the CC will accord to each category of remedy.

We also commend the detail the Draft Guidelines provide as regards the criteria that a remedies package must meet in order to satisfy the CC. Here, we believe that it would assist the business community if the CC were to provide a greater number of examples from its past decisions to illustrate the approach that parties should take. This would reinforce the Draft Guidelines, give greater confidence that the Draft Guidelines are in line with established precedent and that they will be applied consistently. The Draft Guidelines currently provide only a relatively limited number of such examples.

Weaknesses in behavioural remedies

The CC explains in welcome detail the potential risks associated with behavioural remedies at paragraph 4.2 of the Draft Guidelines. However, we note that the CC also articulates in paragraphs 4.5 and 4.6 of the Draft Guidelines further factors relating to the effective enforcement of behavioural remedies which we do not believe are appropriate for the CC to take into consideration. These are:

- (a) the “*constraints on the OFT’s resources and the possible limitations... on the reporting role of customers and competitors*” (paragraph 4.5); and
- (b) the preference for the CC to use its own remedial measures over the *ex post* enforcement of competition law (paragraph 4.6).

We do not believe that it is appropriate for the CC to compensate for what it may believe to be failings in the OFT’s effectiveness by imposing more swingeing remedial measures on



the merging parties than would otherwise be the case. Further, we do not believe that the CC is correct in disregarding the disciplining effect of *ex post* enforcement of competition law when considering remedies, bearing in mind the Court of Justice's ruling in *Tetra Laval*, where *ex post* enforcement was taken into consideration.

These statements reflect the apparent importance that the CC accords to ensuring the absolute effectiveness of a remedy, as noted above, and may lead to a disproportionate outcome in certain cases because (i) not only will parties have to offer more by way of remedies as a result; but (ii) they will still be exposed to enforcement action from the OFT and *ex post* enforcement of competition law.

We believe it is fair for merging parties subject to the UK merger control regime to assume that UK competition laws will be applied effectively and efficiently, and to be treated by all UK regulators on the basis of this assumption. It would be extraordinary if supranational regulators with jurisdiction over a merger affecting the UK, such as the EC Commission, sought to impose harsher remedies for competition concerns in the UK than elsewhere, because of reservations as to the OFT's effectiveness. It is difficult to believe that the CC would advocate such a position, and we would welcome further clarification on this issue.

Recommendations to Government

We have similar concerns in relation to the position taken in the Draft Guidelines on recommendations to Government. We note that the CC will in future consider "*the likelihood of whether such recommendations will be adopted*" (paragraph 2.22). We do not believe that it is appropriate for the CC to seek to intervene in a transaction where the potentially adverse effects that it may give rise to could be adequately or better addressed by Governmental action to address market wide issues. Such an approach gives rise to the risk that market development could be further distorted or hindered as a consequence of the CC's unwarranted intervention. It is another example of the need for a more balanced and less absolutist approach to the effectiveness of a remedy.

In any event, it is not clear how the CC intends to make this assessment in view of the fact that its jurisdiction is limited to the review period granted under the Act, whereas the legislative process is a longer run affair. Will the CC, for example, seek evidence from the relevant Government department, or will it expect the merging parties to provide evidence from the relevant Government department that a recommendation from the CC, if it were to



be made, would be acted upon? It is not clear that either approach is practical, and we would therefore welcome further clarification on this issue.

Suitable Purchasers

We note the greater detail provided in the Draft Guidelines as to the criteria that will need to be satisfied by a possible purchaser of a divestment asset. The increased transparency brought about by this explanation is welcome.

We have concerns, however, that it may set too high a threshold for potential purchasers to satisfy in certain cases, thereby unnecessarily limiting the pool of potential purchasers available to the merging parties and, ultimately, the CC. For example, it is not clear that a highly leveraged acquisition of a divestiture package would not meet the CC's "capability" criteria (paragraph 3.15(b)). The very high levels of transactional activity undertaken by private equity firms in recent years provide strong evidence that any presumption that high levels of leverage will reduce scope for investment in the business is unwarranted.

Indeed, the CC may take the view that a reputable 'financial' buyer may in some cases be more likely to pursue an aggressively competitive strategy than a purchaser found from the seller's contacts in the trade.

Relevant customer benefits

We note the CC's proposed guidance in relation to taking into account "relevant customer benefits" deriving from the merger. It is necessary, however, for the CC to clarify its understanding of what is meant by "relevant customers" under the Act. Otherwise, we believe that it will be difficult for merging parties to prepare evidence to meet the CC's requirements.

It is also not clear from the Draft Guidelines what the CC's counterfactual would be against which the relevant customer benefits would be assessed. We note that one such counterfactual would be the status quo ante, but we also note that the Draft Guidelines indicate that there may be other appropriate counterfactuals e.g. alternative arrangements, such as access arrangements. This is an area on which greater certainty would be welcome in order to promote a consistent approach.



We would also welcome greater clarity as regards what the CC would consider to be a “reasonable expectation” that prospective cost reductions would result (paragraph 1.18).

We hope that the CC will find these comments useful in framing its final guidelines. We would of course be happy to clarify further these points or provide further information should the CC find it helpful.

Yours sincerely

Nicholas Spearing