

MERGER FEES

Consultation on possible
changes to the system of
charging firms for the
costs of merger control

CONSULTATION DOCUMENT

AUGUST 2004

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Charging for the costs of merger control

This consultation document seeks your views on possible changes to the system of charging firms for the costs of merger control.

The charging system was introduced in 1990 on the basis that the amount recovered should broadly equate to the administration costs of the competition authorities. But fee levels have not been increased since their introduction and income now falls significantly below costs. This shortfall is currently being met by the taxpayer.

The Government therefore wants to review the fee system and is inviting views from business and any other interested parties on a range of options, including:

- whether to move to full cost recovery, and if so how; and
- a range of possible fee structures.

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Respond by 3 November 2004

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1. Executive Summary

Purpose of the consultation

This consultation document seeks your views on possible changes to the system of charging firms for the costs of merger control.

The system of charging firms for the costs of merger control was introduced in October 1990, with the Secretary of State for Trade and Industry responsible for setting the level of fees and for determining the relevant costs to be taken into account for that purpose. It was designed so that the amount recovered should broadly equate to the average annual costs of the Department of Trade and Industry, the Office of Fair Trading and the Competition Commission in administering merger control.

Income from merger fees has, however, fallen significantly below costs on a regular basis. This is due to a number of factors: the original fee levels set were below full cost recovery which meant that the system began from a position of deficit; fee levels have not been increased since their introduction so no account has been taken of inflation over the past 14 years; and costs of the regime have increased in order to ensure that a world class framework for competition is put in place. This shortfall is currently being met by the general taxpayer, and could be taken as running against the Government's policy of achieving full cost recovery for statutory services.

The Government has therefore decided to undertake a review of the fee system, and this consultation is intended to ensure that the views of business and other interested parties can be taken fully into account.

Questions for consultees

The following questions relate to specific issues on which we would welcome views:

Question 1 - Would an increase in fees be appropriate and, if so, should this be to achieve (a) full cost recovery straight away or in a phased approach or (b) merely greater cost recovery?

Question 2 – If a phased approach to the introduction of full cost recovery is taken, how best might this be done?

Question 3 - Should fees be charged for material influence cases?

Question 4 - Should fees be charged in special merger situations or cases considered under Article 21(4) of the EC Merger Regulation?

Question 5 - What merits and drawbacks do you see with the following options for a possible future fee structure, and which would be your preferred option?

- Option 1 - Flat fee
- Option 2 - Banded fee based on the turnover of the acquirer, using turnover bands currently in place.
- Option 3 - Banding of fee based on turnover of the acquirer, using new bands with greater differentiation between larger acquisitions.
- Option 4 - Flat fee for all qualifying mergers, with an additional fee for those mergers referred to the Competition Commission for further investigation
- Option 5 - Banding of fee based on turnover of the acquirer, with an additional banded fee for those cases referred for further investigation to the Competition Commission.

Each of these options is set out in more detail in Chapter 3, with specific fee levels given for both greater cost recovery (based on inflation only increases to the original levels set in 1990) and full cost recovery as calculated using 2002/03 figures. The cost of administering merger control in future years under the Enterprise Act is expected to be significantly higher. This will lead to higher levels for full cost recovery than those set out in this consultation document and needs to be borne in mind when responding to the consultation.

We would also welcome comments on other aspects of the fees regime, such as suggestions of other ways in which the system might be improved.

Responses and closing date

You can respond to this consultation by e-mail to:

Ian.Lomas@dti.gsi.gov.uk

or by post to:

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Responses should be received by **3 November 2004**. We are also very happy to meet with individuals or organisations to discuss possible changes to the fees regime. Any queries about meetings, or general policy queries on this topic, should also be directed to the address above.

A summary of the consultation responses and outcome will be provided on <http://www.dti.gov.uk/ccp/consultations.htm> by January 2005.

Disclosure of responses

Your response to this consultation document may be made publicly available in whole or in part at the Department's discretion. If you do not wish all or part of your response or your name to be made public, you must indicate in your response what you wish us to keep confidential. Any e-mail response sent from a corporate system may carry an automatically generated notice stating that the content of the message should be treated as confidential. Where you do not wish your views to be treated as confidential, please make it clear that such an automatically generated message does not apply.

Consultees

This consultation document is available at <http://www.dti.gov.uk/ccp/consultations.htm>. It is also being sent to the consultees listed in section 5 of this consultation document. Please tell us if you know of others who would be interested in receiving a copy. The document may be photocopied without prior permission. Additional copies can be obtained by calling 020 7215 6460.

Help with queries

The Department seeks where possible to abide by the Cabinet Office's Code of Practice on Written Consultation. A copy of the Code's Consultation Criteria is at Annex A to this document. If you wish to comment on the conduct of this consultation or make a complaint about the way this consultation has been conducted, please write to Nick van Benschoten, DTI Consultation Co-ordinator, Room 723, 1 Victoria Street, London SW1H 0ET or telephone him on 020 7215 6206 or mail to: nick.vanbenschoten@dti.gsi.gov.uk

2. Background

Case for reviewing the merger fees system

2.1 The Government's policy is that fee levels should normally be set to recover the full cost of the service calculated in accordance with the Fees and Charges Guide¹, while recognising in some cases that it may not be appropriate. The Guide explains that the purpose of this is to "ensure that resources are allocated efficiently". In addition, recovery of the full costs of a service ensures that the general taxpayer is relieved of costs which are more properly borne by users who benefit directly from the service.

2.2 Merger control costs of the competition authorities have generally increased year on year. This is due primarily to inflation, and also to ensure that a world class framework for competition is put in place. However, with no corresponding increase in fee levels, income has tended to fall short of costs. In only one year, 1993/94, have costs been covered by income. A deficit has been incurred in all other years since 1990, ranging from around £800,000 in the early years of the fee regime to over £2million in 2001/02 and 2002/03². Data for 2003/04 has just been made available and this shows that total costs were some £15.68 million (of which around £12 million relates to chargeable services). This is not a typical year for costs due to various factors, such as the transition to the Enterprise Act regime and has not, therefore, been used as the basis for the illustrative calculations contained in this consultation document. It does indicate, however, that costs are likely to be considerably higher in future than in 2002/03.

2.3 Clear reasons exist for exempting SMEs³ from paying merger fees, and there is no intention at present to reverse this exemption. Similarly, the legal complexities of attempting to charge acquirers not established in the UK mean that it is not proposed to consult on charging such entities.

2.4 There are two types of merger situation - material influence cases and special merger situations - where no fee is payable at present. However, such cases qualify for consideration under the Enterprise Act and it is not clear that there remains a justification for excluding such cases from the requirement to pay a fee.

2.5 With these points in mind the then Competition Minister, Melanie Johnson, announced on 28 January 2003 that a full review of the fee system would be undertaken once the Enterprise Act merger regime was up and running.

¹ See Section 2 of "The Fees and Charges Guide (1992)" – HM Treasury.

² Fees collected by the OFT in 2002/03 of £2.09 million, against total chargeable Government costs of implementing the UK mergers regime of £4.35 million (the total cost of administering merger control was £6 million. About 72.5% of work conducted was on chargeable cases. The remaining time was spent on non-statutory services and cases for which fees were not payable). In 2002/03 there were 162 cases qualifying mergers, with a fee payable in 152 of these cases. In the same period, the Competition Commission completed 12 merger inquiries.

³ See section 5, footnote 19 of this document for definition of SME.

The regime has been operation for a year and the commencement of the review would now seem appropriate.

2.6 A preliminary consultation has already been undertaken on an informal basis with a selection of key stakeholders over the last 9 months or so. Views from this have been used to help identify the possible options for change set out in the following section.

Origins of the fees regime for merger control

2.7 The system of charging firms for the costs of merger control was introduced in October 1990 under the Mergers (Fees) Regulations 1990. Fees were payable to the Office of Fair Trading in respect of mergers which qualified for investigation under the Fair Trading Act 1973.

2.8 The rationale behind the system's introduction was:

- the general principle of Government Accounting that the cost of providing services to non-Exchequer bodies should be charged at a suitable rate to cover costs;
- the principle that costs of merger control should be recovered from users rather than through general taxation;
- a specific need to recover the costs of procedural improvement to the competition regime introduced in the late-1980s.

2.9 As a "statutory service" (ie one where there was provision in statute to recover a fee for a service), the system's main objective was to achieve full cost recovery (but not a surplus) of merger control costs from the fees charged.

2.10 The fees regime was designed to be easy to operate, with a simple charging structure aimed at cost recovery on an overall basis. However, it was not intended to reflect the amount of work involved or costs actually incurred for any one case. Fees were paid by the acquiring company or its parent, but the fee level depended upon the size of the target company. Charges were made as follows, with the aim of achieving close to full-cost recovery:

Value of gross assets acquired £30 million or less	£5,000
Value of gross assets acquired over £30 million but not over £100 million	£10,000
Value of gross assets exceeds £100 million	£15,000

2.11 Fees were also payable for an application for the Secretary of State's consent to the transfer of a newspaper or newspaper assets, and on the making of a merger reference under the Water Industry Act 1991.

2.12 In June 2001, the Secretary of State brought in regulations to exempt small and medium enterprises (SMEs) from paying statutory merger fees. This was introduced to help in reducing the burdens on business and to encourage a vigorous small company sector.

Current Position

2.13 Merger law was reformed by the Enterprise Act 2002, which came into force on 20 June 2003. The Act made very few changes of direct relevance to the fees regime; the main one being the replacement of the assets-based qualifying threshold with one based on turnover. This was done because turnover was seen as a better indicator of the commercial value of an enterprise in today's economy. A fee charging system for the new legislation was enacted through the Enterprise Act 2002 (Merger Fees and Determination of Turnover) Order 2003⁴, and means that fees are now charged according to the level of turnover of the enterprises being acquired. The actual level of fees was not increased, and turnover bands were set at levels which it was thought would achieve approximately the same level of cost recovery as was achieved under the Fair Trading Act regime. Indeed, the level has remained unchanged since their introduction in 1990. As the following table shows, fee levels would have been significantly higher if they had increased each year in line with inflation:

	Current	Annual inflation increase
Acquirer is an SME	0	-
Value of UK turnover of enterprises acquired £20 million or less	£5,000	£7,372
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£10,000	£14,743
Value of UK turnover of enterprises acquired exceeds £70 million	£15,000	£22,115

2.14 Subject to some limited exceptions, a merger which qualifies for investigation under the standard merger provisions of the Enterprise Act is subject to a fee irrespective of whether a reference to the Competition Commission is made. The main exceptions relate to: acquisition of less than a controlling interest where a merger notice has not been submitted in relation to that acquisition (known as a material influence case); acquisition made by a company not established in the UK unless the creation of the relevant merger situation results wholly or partially from anything done by him in the UK (for example, if the transaction was actually completed in the UK); and acquisitions by SMEs. In addition, no fee is currently payable for mergers which qualify for investigation under the special merger regime.

Merger fees in other jurisdictions

⁴ The Merger (Fees) Regulations 1990 are still in force for the merger of water or sewerage undertakings. However, these will be repealed once the water provisions of the Enterprise Act are commenced.

2.15 Wide variations exist in the approaches taken by different national competition bodies in charging for merger control. In some cases, no merger fee is charged: for example, in 2003/04 the European Commission and 9 of its then 15 member states⁵ did not charge. Where a fee is charged, the following table shows that no consistent approach exists on the threshold for charging or the level of the fee. Current charges in the UK are lower than those for most other jurisdictions where a fee is charged.

Jurisdiction	Details of fee charged by competition authority⁶
Germany	Fee usually not to exceed EUR 50,000 (approx £34,600), with level determined according to costs incurred by the competition authority, and the economic significance of the concentration. In exceptional larger transactions EUR 100,000 (£69,200). In the last three years (2001-2003) merger fees of more than 50,000 Euro have been charged in three cases each year.
Spain	EUR 3,005 (£2,000) to 60,000 (£41,500) depending on turnover of companies involved
Ireland	EUR 8,000 (£5,500) for all mergers exceeding a turnover of EUR 40 million (£27m)
Austria	EUR 750 (£500) for a merger notification; variable charge of EUR 1,500-30,000 (£1,000 - £20,700) for phase 2 cases
Portugal	EUR 7,500-25,000 (£5,100 - £17,200) depending on turnover of the companies concerned, with additional amount payable if detailed investigation is undertaken
Australia	AUD \$15,000 (£5,900)
Canada	CDN \$50,000 (£21,800)
New Zealand	\$950 to \$9,494 (£300 - £3,600)
US	\$45,000 (£27,500) for reportable acquisitions valued at below \$100 million (£61m) \$125,000 (£76,400) for acquisitions valued at between \$100 million and \$500 million (£61m - £305m) \$280,000 (£171,200) for acquisitions valued at more than \$500 million (£305m)

⁵ Belgium, Denmark, Greece, France, Italy, Luxembourg, Netherlands, Finland, Sweden

⁶ Data compiled March 2004

3. Options for change

3.1 This consultation provides an opportunity to undertake a wide-ranging review of the merger fees regime and the types of mergers in which a fee is payable. From informal discussions with a selection of key stakeholders over the last 9 months, the Government has identified five main areas of possible change. These are set out in the following pages, with associated questions on which responses from consultees would be welcome. The Government also welcomes any comments on other aspects of the fees regime.

(i) Basis for charging

3.2 As explained in Chapter 2, the Government's policy is that fee levels should normally be set to recover the full cost of a service. The system of charging for merger control was introduced in 1990 on this basis, but the level of income now falls significantly below that of costs. The Government is not currently aware of a compelling argument not to move to full-cost recovery, at least through a phased approach

Question 1 - Would an increase in fees be appropriate and, if so, should this be to achieve (a) full cost recovery straight away or in a phased approach or (b) merely greater cost recovery, with the increase set to take account of inflation levels since 1990?

3.3 A phased approach to the introduction of full cost recovery might be achieved in several ways. For example, this might be done simply by increasing fees each year so that an increasing percentage of costs would be recovered over time i.e 60% of costs recovered in year one, 70% in year two and so on until full cost recovery is achieved. Alternatively, fees might be increased each year by inflation + a specific amount until full cost recovery had been achieved. The first option would rely on being able to make a reasonably accurate prediction at the beginning of the year of the forthcoming costs of the competition authorities and the number of merger cases which they would need to consider. The second option would provide greater certainty as to the level of fees to be incurred in the future.

Question 2 - If a phased approach to the introduction of full cost recovery is taken, how best might this be done?

(ii) Material Influence Cases

3.4 No charge is made at present for mergers where only material influence over the target is acquired. The Government's policy is that there should be legal certainty for companies considering a transaction as to whether they would incur a merger fee. The OFT's publication *Mergers – substantive assessment guidance* (available on its website at www.of.gov.uk) contains guidance on what represents material influence. In addition, there are an increasing number of OFT decisions published on their website dealing with the question of jurisdiction in cases.

However, assessment of material influence requires a case by case analysis of the entire relationship between the acquiring entity and the target, and the variety of commercial arrangements entered into makes it difficult to state categorically in advance what will (or will not) constitute material influence. Despite this lack of absolute certainty in advance on what represents material influence, it could be argued that a case which is caught by the jurisdictional rules should incur a charge, particularly as either the general taxpayer or other merger cases would otherwise have to meet the costs.

3.5 In the preliminary consultation there was some support for this. Arguments included that the uncertainty of whether a fee would be charged was smaller than the uncertainty caused by the possibility of having the merger blocked or unwound, and that whether a deal results in material influence being acquired is something that you know when you see.

Question 3 - Should fees be charged for material influence cases?

(iv) Special merger situations and cases considered under Article 21(4) of the EC Merger Regulation

3.6 Merger fees are currently payable in relation to a relevant merger situation. However, the Enterprise Act also allows the Secretary of State to intervene in mergers which do not meet the qualifying thresholds for the standard merger regime if she believes that any of the public interest considerations are relevant (currently national security, and considerations relevant to newspaper, broadcasting and cross-media mergers). The Secretary of State is also able to intervene on public interest grounds in cases falling for consideration under the EC Merger Regime through the use of Article 21(4) of the EC Merger Regulation. There is no competition assessment in special merger situations, and no competition assessment undertaken in the UK in Article 21(4) cases. The Secretary of State will consider whether to refer such transactions to the Competition Commission solely on public interest grounds. No fee is currently payable in such cases.

3.7 In the preliminary consultation there were mixed views on charging for special merger cases. Some were in favour of charging: if a merger required regulatory scrutiny for whatever reason, then a fee should be payable. Others were against charging: there were suggestions that these cases raised non-competition issues which fall to the Government, so it was difficult to predict whether a merger would warrant intervention and therefore whether a fee would be payable. This would go against the up-front certainty as to regulatory cost which most consultees thought was an important feature for a merger regime. Similar arguments apply to Article 21(4) cases. A further consideration may be that the European Commission does not charge a fee for the competition assessment which it undertakes on cases notified under the EC Merger Regulation.

Question 4 - Should fees be charged in special merger situations or cases considered under Article 21(4) of the EC Merger Regulation?

(iv) Future fee structure

3.8 The Government has identified five broad options for a possible future fee structure. The actual fee levels given against the various options are calculated on the basis of achieving a greater level of cost recovery (possibly as a first step to full-cost recovery) and full cost recovery and assume that a fee is charged for all relevant merger situations and special merger situations. Greater cost recovery figures are based on a year-on-year inflation increase. Those for full cost recovery have been calculated using costs and numbers of cases for 2002/03, the latest year for which full data is available. The cost of implementing the merger regime under the Enterprise Act is expected to be significantly greater, and therefore the fees needed to achieve full-cost recovery under the new regime are expected to be significantly higher.

Option 1: Flat fee for all qualifying mergers of (i) £17,000⁷ for greater level of cost recovery, or (ii) £28,000⁸ for full cost recovery.

Option 2: Banded fee based on the turnover of the enterprise acquired, using turnover bands currently in place.

	Inflation only increase	2002/03 full cost recovery
Value of UK turnover of enterprises acquired £20 million or less	£7,500	£15,000
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£15,000	£25,000
Value of UK turnover of enterprises acquired exceeds £70 million	£22,500	£35,000

Option 3: Banding of fee based on turnover of the enterprise acquired, using new bands with greater differentiation between larger acquisitions.

	Greater cost recovery	2002/03 full cost recovery
Value of UK turnover of enterprises acquired	£7500	£7500

⁷ This figure is calculated to generate income of approximately £2.7 million per annum – the level of income which would have been generated if fees levels set in 1990 had been increased each year in line with inflation. ‘Inflation only increase’ fee levels for options 2-5 are based on generating the same level of income.

⁸ This figure is calculated to generate income of approximately £4.3 million per annum – equivalent to the total chargeable Government costs of implementing the UK mergers regime in 2002/03.

£20 million or less		
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£12500	£17500
Value of UK turnover of enterprises acquired over £70 million but not over £100 million	£17500	£22500
Value of UK turnover of enterprises acquired over £100 million but not over £200 million	£22500	£40000
Value of UK turnover of enterprises acquired exceeds £200 million	£27000	£47500

Option 4: Flat fee for all qualifying mergers of £12500 for greater level of cost recovery, or £15000 for full cost recovery, with an additional fee for those mergers referred to the Competition Commission for further investigation of £75000 for greater level of cost recovery, or £225000 for full cost recovery.

Option 5: Banding of fee based on turnover of the enterprise acquired, with an additional banded fee for those cases referred to the Competition Commission for further investigation.

	Greater cost recovery	2002/03 full cost recovery
Value of UK turnover of enterprises acquired £20 million or less	£5000 plus £50000 if referred	£7500 plus £75000 if referred
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£10000 plus £60000 if referred	£15000 plus £125000 if referred
Value of UK turnover of enterprises acquired over £70 million but not over £100 million	£15000 plus £75000 if referred	£22500 plus £175000 if referred
Value of UK turnover of enterprises acquired over £100 million but not over £200 million	£17500 plus £100000 if referred	£25000 plus £250000 if referred
Value of UK turnover of enterprises acquired exceeds £200 million	£20000 plus £125000 if referred	£30000 plus £300000 if referred

3.9 The remainder of this section sets out possible arguments for and against each of the five options identified for achieving greater cost recovery.

Option 1: Flat fee

Arguments in favour of this option

- Provides upfront certainty for acquirer of costs involved
- Simple charging structure which is easy to administer

- Wide distribution of costs accurately reflects view that merger regulation benefits the market and the economy as a whole.

Arguments against this option

- Possibly unfair that size of transaction not taken into consideration
- Size of fee might undermine the rationale for smaller transactions, including those caught by the special merger regime
- Level of work undertaken by the competition authorities for a particular case not taken into consideration

Option 2: Banded fee based on the turnover of the enterprise acquired, using turnover bands currently in place.

Arguments in favour of this option

- Provides upfront certainty for acquirer of costs involved
- Straightforward charging structure which is relatively easy to administer
- Reasonably wide distribution of costs reflects view that merger regulation benefits the market and the economy as a whole.
- Weights fee to reduce impact on smaller acquisitions which might undermine their rationale

Arguments against this option

- Level of work undertaken by the competition authorities on a particular case not taken into consideration
- All mergers which meet the turnover qualifying threshold are charged the same amount, so size of transaction only partially taken into account in fee structure. Could be considered disproportionately high on smaller companies.

Option 3: Banding of fee based on turnover of the enterprise acquired, using new bands with greater differentiation between larger acquisitions.

Arguments in favour of this option

- Provides upfront certainty for acquirer of costs involved
- Straightforward charging structure which is relatively easy to administer
- Reasonably wide distribution of costs reflects view that merger regulation benefits the market and the economy as a whole.
- Weighting of fee to reduce impact on smaller acquisitions, and attributes higher fees to the most economically important acquisitions

Arguments against this option.

- Level of work undertaken by the competition authorities on a particular case not taken into consideration

Option 4: Flat fee for all qualifying mergers, with an additional fee for those mergers referred to the Competition Commission for further investigation

Arguments in favour of this option

- At least partially reflects level of input from different competition authorities into individual cases
- In comparison to reference cases, ensures a lower fee for those mergers where little or no competitive overlap exists

Arguments against this option

- Parties already face additional time and legal costs from reference
- If CC charge fully or substantially reflects actual cost of CC inquiry then likely to undermine rationale for some acquisitions and result in more of those cases that have been referred being abandoned
- No upfront certainty for acquirer of costs involved
- Not necessarily straightforward to administer
- Does not take account of the view that merger regulation benefits the market and the economy as a whole.

Option 5: Banding of fee based on turnover of the enterprise acquired, with an additional banded fee for those cases referred for further investigation to the Competition Commission.

Arguments in favour of this option

- At least partially reflects level of input from different competition authorities into individual cases
- In comparison to reference cases, ensures a lower fee for those mergers where little or no competitive overlap exists
- Some weighting of fee to reduce impact on smaller acquisitions

Arguments against this option

- Parties already face additional time and legal costs from reference
- If CC charge fully or substantially reflects actual cost of CC inquiry then likely to undermine rationale for some acquisitions and result in more of those cases that have been referred being abandoned
- No upfront certainty for acquirer of costs involved
- Not necessarily straightforward to administer
- Does not take account of the view that merger regulation benefits the market and the economy as a whole
- Most complicated option to administer.

Question 5 - What merits and drawbacks do you see with the options set out above for a possible future fee structure, and which would be your preferred option?

Question 6 - Are there any other ways in which the merger fees regime might be improved?

4. *What happens next?*

4.1 In the light of responses to this consultation, the Secretary of State will consider what changes, if any, should be made to the fees regime for merger control. The intention would be to introduce these by April 2005.

5. Draft Regulatory Impact Assessment

Proposal

To amend the Enterprise Act 2002 (Merger Fees and Determination of Turnover) Order 2003 to move towards full cost recovery for the merger control regime, as calculated in accordance with the Fees and Charges Guide⁹.

Issue

The Government's policy is that fee levels for statutory services should normally be set to recover the full cost of the service calculated in accordance with the Fees and Charges Guide, while recognising in some cases that it may not be appropriate.

The system of charging firms for the cost of merger control was introduced in October 1990. With limited exceptions, a fee is payable for any merger which qualifies for investigation by the Office of Fair Trading (OFT) under the Enterprise Act 2002. Merger control costs of the competition authorities have increased year on year since their introduction, but there has been no increase in fee levels. Income has therefore consistently fallen short of costs on a regular basis (see Risk Assessment section below). No clear justification has been made why the general taxpayer, rather than the businesses concerned, should meet this shortfall.

There are three types of merger situation - material influence cases¹⁰, special merger situations¹¹ and Article 21(4) cases¹² - where no fee is payable at present. However, such cases qualify for consideration under the Enterprise Act and it is not clear that there remains a justification for excluding such cases from the requirement to pay a fee.

Objective

The objective of the proposed amendments is therefore to revise the merger fees regime so that the basis for charging and the level of fees benefit the economy as a whole. This means that the interests of general taxpayers and all the businesses concerned need to be properly balanced. The Government's view is that mergers contribute to an efficient economy provided they do not undermine competition. It would not, therefore, wish to take actions which would prevent a merger unless it was expected to result in a substantial lessening of competition.

⁹See Section 3 of "The Fees and Charges Guide (1992)" – HM Treasury.

¹⁰ Acquisition of less than a controlling interest where a merger notice has not been submitted by the parties to the OFT in relation to that acquisition.

¹¹ The Enterprise Act allows the Secretary of State to intervene in mergers which do not meet the qualifying thresholds for the standard merger regime if she believes that any of the public interest considerations are relevant.

¹² The Secretary of State is also able to intervene on public interest grounds in cases falling for consideration under the EC Merger Regime through the use of Article 21(4) of the EC Merger Regulation.

Risk Assessment

The disparity between the costs of the merger control regime and the level of fees collected has resulted in the Exchequer incurring deficits of over £2 million in 2002/03. Indeed, a deficit of over £800,000 has been incurred in all but one year since 1990. The impact of inflation and changes to how mergers are considered mean that this disparity will increase significantly under the Enterprise Act regime. Without a move towards full cost recovery, the Exchequer – and in turn the general taxpayer – will need to meet the resulting shortfall.

One possible detriment would result from a decision not to charge for consideration of material influence cases, special merger situations and cases considered under Article 21(4) of the EC Merger Regime. If merger fees are not increased in the future, any deficits will, as now, need to be borne by the general taxpayer. Previous experience suggests that there might be a total of around 6 such cases each year¹³, with an average cost per case for regulatory consideration of £28,000. This means that the detriment to the general taxpayer could be in excess of £150,000 per year¹⁴.

Options

Options for change to the merger fees regime fall into three broad areas: move to full cost recovery; the extension of charging; and structure of fees. The specific options are set out below, with the benefits and costs of each considered in the following section.

(1) Move to full cost recovery

Option 1(a): To make no changes to the basis for charging, so that current charges would apply

Option 1(b): To move to greater cost recovery, but not full cost recovery

Option 1 (c): To move to full cost recovery in a phased approach

Option 1(d): To move straight away to full cost recovery

(2) Extension of charging

Option 2(a): Charging for material influence cases

¹³ In 2002/03, the OFT investigated three material influence cases. There have been no special merger situations since the Enterprise Act came into force on 20 June 2003, and the number of such future cases is expected to remain very small. For the purposes of this consultation, it is assumed that there will be one special merger situation each year. The number of Article 21(4) cases has varied over time, but on average there might be around two per year.

¹⁴ Although there are also benefits to the consumer in operating this regime.

Option 2(b): Charging for special merger situations and cases considered under Article 21(4) of the EC Merger Regime

(3) Fee structure

Option 3(a): Flat fee for all qualifying mergers of (i) £17,000¹⁵ for greater level of cost recovery, or (ii) £28,000¹⁶ for full cost recovery.

Option 3(b): Banded fee based on the turnover of the enterprise acquired, using turnover bands currently in place.

	Inflation only increase	2002/03 full cost recovery
Value of UK turnover of enterprises acquired £20 million or less	£7,500	£15,000
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£15,000	£25,000
Value of UK turnover of enterprises acquired exceeds £70 million	£22,500	£35,000

Option 3(c): Banding of fee based on turnover of the enterprise acquired, using new bands with greater differentiation between larger acquisitions.

	Greater cost recovery	2002/03 full cost recovery
Value of UK turnover of enterprises acquired £20 million or less	£7500	£7500
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£12500	£17500
Value of UK turnover of enterprises acquired over £70 million but not over £100 million	£17500	£22500
Value of UK turnover of enterprises acquired over £100 million but not over £200 million	£22500	£40000
Value of UK turnover of enterprises acquired exceeds £200 million	£27000	£47500

Option 3(d): Flat fee for all qualifying mergers of £12500 for greater level of cost recovery, or £15000 for full cost recovery, with an additional fee for those mergers referred to the Competition Commission for

¹⁵ This figure is calculated to generate income of approximately £2.7 million per annum – the level of income which would have been generated if fees levels set in 1990 had been increased each year in line with inflation. ‘Inflation only increase’ fee levels for options 3(b)-(e) are based on generating the same level of income.

¹⁶ This figure is calculated to generate income of approximately £4.3 million per annum – equivalent to the total chargeable Government costs of implementing the UK mergers regime in 2002/03.

further investigation of £75000 for greater level of cost recovery, or £225000 for full cost recovery.

Option 3(e): Banding of fee based on turnover of the enterprise acquired, with an additional banded fee for those cases referred to the Competition Commission for further investigation.

	Greater cost recovery	2002/03 full cost recovery
Value of UK turnover of enterprises acquired £20 million or less	£5000 plus £50000 if referred	£7500 plus £75000 if referred
Value of UK turnover of enterprises acquired over £20 million but not over £70 million	£10000 plus £60000 if referred	£15000 plus £125000 if referred
Value of UK turnover of enterprises acquired over £70 million but not over £100 million	£15000 plus £75000 if referred	£22500 plus £175000 if referred
Value of UK turnover of enterprises acquired over £100 million but not over £200 million	£17500 plus £100000 if referred	£25000 plus £250000 if referred
Value of UK turnover of enterprises acquired exceeds £200 million	£20000 plus £125000 if referred	£30000 plus £300000 if referred

Benefits and costs

The benefits and costs of each option are set out below. In summary, the key benefit from increasing the level of fees charged is that the general taxpayer would no longer have to meet these costs. The economic rationale of some smaller transactions might be jeopardised by a move to full cost recovery with no weighting of fees.

(1) Move to full cost recovery

Whilst it is impossible to predict accurately the future costs of merger control or the level of income derived from merger fees, the deficit between income and costs has not been less than £940,000 since 1993/94.

None of the options involve a significant net cost. These proposals involve varying degrees of transfer of the cost of merger investigations from the general taxpayer to the merger parties. With some of the options, there may be the potential for some distortion in merger activity.

Option 1 (a), the status quo, implies the Government continues to incur the majority of the costs of merger investigations (over £2 million in 2002/03). Merging parties therefore do not bear the true cost of their activities.

Options 1(b) and (c) offer a hybrid approach, with the general taxpayer meeting around £2 million of the shortfall.

One possible detriment from option 1(d) and, once full cost recovery is reached from option 1(c), is that they may have the potential to act as a disincentive to merge. This could impact negatively both in terms of innovation and efficiency as well as on total welfare. The impact is likely to be greatest where the turnover of the enterprise being acquired is small. In 2002/03 the level of turnover of the enterprises being acquired ranged from £340,000 to at least £282 million. In 37 cases, turnover was less than £20 million, and it is conceivable that a move to full cost recovery might be seen as jeopardising the economic rationale of the smallest of these transactions. This might be the case particularly where the fee structure did not include an element of banding.

(2) Extension of charging

Option 2(a) & 2(b) - the benefit to be gained from charging a fee for material influence cases and special merger situations is that it will ensure that the general taxpayer is not paying a contribution towards operating it. This would result in a saving of around £100,000 per year (depending on the structure and level of fees introduced).

The collection of fees in these cases should be no more complex than for others so should not involve additional administration costs.

(3) Fee structure

Option 3(a) - This would provide upfront certainty for the acquirer of the costs involved, and a simple charging structure for the OFT to administer. The wide distribution of costs involved accurately reflects the view that merger regulation benefits the market and the economy as a whole.

As noted above, the lack of any banding might jeopardise the economic rationale of some mergers, with a higher impact on the acquisition of smaller enterprises. This could present a cost disadvantage to the enterprises who would otherwise have taken forward the merger, although the actual detriment would presumably be no more than the actual fee level. The charging of a single fee does not allow the level of work undertaken by the competition authorities in considering the merger to be taken into account.

Options 3(b) and 3(c) – These have most of the same benefits and costs of Option 3(a). However, the impact on smaller acquisitions is reduced by the weighting of fees and in so doing reducing the incidence of economic impact.

Option 3(d) and 3(e) – These reflect the level of input from competition authorities into individual cases and ensure a lower fee for those mergers where the Office of Fair Trading identifies little or no competitive overlap. It could therefore be argued that, for these cases at least, both options are generally pro-competitive. Option 3(e) also has the benefit of reducing the impact on smaller acquisitions of any increase, at least to some extent, by the weighting of fees.

The main detriment associated with either option is that it will probably lead to the abandonment of a far greater number of mergers that have been referred to the Competition Commission, even though the Commission may eventually have found that the merger was not anti-competitive. The Commission's costs in completing 12 merger inquiries in 2002/03 varied from £262,000 to £524,000 per case. It is likely that a fee based even on the lowest of these costs would seriously impact on the economic rationale of some mergers, particularly given that the parties to a merger already incur additional costs of their own from a reference such as increased legal fees and management time. A further detriment is that these options would be the least straightforward for OFT to administer, although any additional administration costs should not be significant.

Business sectors affected

Merger activity takes place across virtually all business sectors. Subject to some limited exceptions, a fee is payable to the Office of Fair Trading for any merger, regardless of business sector, which qualifies for investigation under the Enterprise Act 2002¹⁷. Fees are also payable on the making of a merger reference under the Water Industry Act 1991. Small and medium sized enterprises are exempt from paying fees and there are no plans to change this.

Competition Assessment

Given the breadth of merger activity, the impact of this provision will inevitably affect any business in any market that might be considering engaging in merger activity. Mergers are a key method for organisational growth and change. Most of the options for change to the merger fees regime would not affect some firms substantially more than others as the weighting of fees should ensure that smaller transactions are not discouraged. For those options where no element of

¹⁷ A merger must meet all three of the following criteria to constitute a relevant merger situation:

- two or more enterprises must cease to be distinct, or there must be arrangements in progress or in contemplation which will lead to enterprises ceasing to be distinct;
- either the merger must not yet have taken place or have taken place not more than four months before the reference is made, unless the merger took place without having been made public and without the OFT being informed of it; and
- either:
 - the UK turnover associated with the enterprise which is being acquired exceeds £70 million, or
 - the enterprises which cease to be distinct supply or acquire goods or services of any description and, as a result of the merger, together supply or acquire at least 25 per cent of all those particular goods or services of that kind supplied in the UK or in a substantial part of it.

weighting is included (options 2(a) and (d)), an increase in fees to full cost recovery might be seen as threatening the economic rationale of acquiring smaller businesses. However, such situations are likely to be limited as such a merger could only qualify for investigation on the basis that it enhances a 25% market share.

Merging parties will normally incur a number of costs in completing a merger. As well as the actual purchase price, these may include costs for legal advisers, PR advisers, economic advisers, management time and a merger fee. Acquiring companies do not publish a breakdown of costs, and these will vary greatly from case to case depending on such things as the profile of the companies, and the complexity of legal and economic issues arising. A recent study on the costs to business of multi-jurisdictional merger reviews¹⁸ confirms this wide variance in costs. Our informal discussions with those involved in the process would suggest that merger fees do not tend to represent a large element of these costs at present. This would remain the case with most of the possible options for change and means that they should not significantly affect market structure, restrict innovation or act as a disadvantage to new or potential firms entering a market.

Small Businesses: The Impact Test

Initial soundings from relevant trade associations have indicated that the impact of the various proposals on small businesses is likely to be small. The continuing SME exemption from paying merger fees means that the only possible impact would occur where, as stated above, a larger enterprise is deterred from acquiring a small business because of the level of fee increase. There are likely to be less than a dozen transactions each year which could potentially be affected, and only if full cost recovery is introduced on the basis of no fee weighting or a relatively high starting fee.

The thresholds for qualification as an SME are set out in the Companies Act 1985, as amended¹⁹. One trade association suggested during the preliminary consultation that consideration be given to increasing these in line with any increase in merger fees. Since the suggestion was made the thresholds have, in

Further details on what constitutes a relevant merger situation are given in the OFT guidance “*Mergers Substantive Assessment Guidance*”, Chapter 2.

¹⁸ *A tax on mergers? Surveying the time and costs to business of multi-jurisdictional merger reviews June 2003*. A study commissioned by the International Bar Association and the American Bar Association.

¹⁹ The definition of a company as small or medium-sized is taken from the Companies Act 1985 (as amended by Statutory Instrument 2004/16). To qualify, it must satisfy two or more of the following:

Small company	Turnover – not more than £5.6m
	Balance sheet total – not more than £2.8m
	Number of employees – not more than 50
Medium-sized company	Turnover – not more than £22.8m
	Balance sheet total – not more than £11.4m
	Number of employees – not more than 250

any case, been increased and no further action is planned in relation to these at this time.

Enforcement, Sanctions, Monitoring and Costs

The OFT is currently responsible for the collection of merger fees and does not report any problems. None of the proposals contained in this consultation document, other than options 2(d) and (e), would involve changing this arrangement. Options 2(d) and (e) would introduce an additional charge for cases referred to the Competition Commission. It would seem sensible that the Commission itself should collect this additional charge. Whilst this would add an extra layer of complexity to the system, the number of cases concerned would be small (probably no more than 12 per year) so the costs should be minimal.

The Department plans to review the new merger fee regime two years after its introduction. The review will consider the level of cost recovery achieved and the impact which the new regime has had on business.

Consultation

[To be inserted in final RIA]

Conclusions and Recommendations

[To be inserted in final RIA]

5. Consultees approached (all by e-mail except where indicated*)

Competition Law Firms:

Addleshaw Goddard
Allen & Overy
Ashurst Morris Crisp
Baker & McKenzie
Bristows
Cleary Gottlieb
Clifford Chance
CMS Cameron McKenna
Davies Arnold Cooper
Eversheds
Freshfields Bruckhaus Deringer
Hammonds
Herbert Smith
Latham & Watkins
Laytons
Linklaters
Lovells
Macfarlanes
Martineau Johnson
Mayer, Brown, Rowe and Maw
McDermott, Will & Emery
Norton Rose
Richards Butler
S J Berwin
S J Melinek
Shearman & Stirling
Simkins Partnership
Simmons & Simmons
Slaughter & May
Stephenson Harwood
Taylor Wessing
Travers Smith Braithwaite
Wragge & Co

Legal Bodies/Individuals:

Competition Law Association
Joint working party of the Bars and Law Societies
Law Society for Northern Ireland
Law Society of Scotland
Monckton Chambers
Richard Whish (Kings College London School of Law)
The City of London Law Society
The Law Society

Tom Sharpe QC

Consumer Organisations:

Consumers' Association
National Consumer Council
Scottish Consumer Council
Welsh Consumers Council

Other Organisations/Bodies:

British Chamber of Commerce in Brussels
British Chambers of Commerce
British Institute of International & Comparative Law
British Retail Consortium
Competition Commission
Confederation of British Industry
Confederation of British Industry Northern Ireland*
Council on Tribunals
Department of Enterprise, Trade and Investment, Northern Ireland*
Federation of Small Businesses
Federation of Small Businesses Northern Ireland*
Forum of Private Business
HM Treasury
Institute of Directors
Institute of Directors Northern Ireland*
Wales IOD
Northern Ireland Chamber of Commerce and Industry
International Chamber of Commerce
Ministry of Defence
Office of Fair Trading
Office of Rail Regulator
OFGEM
OFREG
OFWAT
RBB Economics
Small Business Service
The Newspaper Society
TUC

Copies of this document have also been placed in the House of Lords and House of Commons libraries

ANNEX A

The Consultation Criteria

1. Timing of consultation should be built into the planning process for a policy (including legislation) or service from the start, so that it has the best prospect of improving the proposals concerned, and so that sufficient time is left for it at each stage.
2. It should be clear who is being consulted, about what questions, in what timescale and for what purpose.
3. A consultation document should be as simple and concise as possible. It should include a summary, in two pages at most, of the main questions it seeks views on. It should make it as easy as possible for readers to respond, make contact or complain.
4. Documents should be made widely available, with the fullest use of electronic means (though not to the exclusion of others) and effectively drawn to the attention of all interested groups and individuals.
5. Sufficient time should be allowed for considered responses from all groups with an interest. Twelve weeks should be the standard minimum period for a consultation.
6. Responses should be carefully and open-mindedly analysed, and the results made widely available, with an account of the views expressed, and the reasons for decisions finally taken.
7. Departments should monitor and evaluate consultations, designating a consultation co-ordinator who will ensure the lessons are disseminated. The complete code is available on the Cabinet Office's web site, address <http://www.cabinet-office.gov.uk/servicefirst/index/consultation.htm>.

Comments or complaints

If you wish to comment on the conduct of this consultation or make a complaint about the way this consultation has been conducted, please write to

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