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UK COMPETITION LAW

**Modernisation - a consultation
on the Government's proposals
for exclusions and exemptions
from the Competition Act 1998
in light of Regulation 1/2003 EC**

June 2003

FOREWORD BY GERRY SUTCLIFFE, PARLIAMENTARY UNDER SECRETARY OF STATE FOR EMPLOYMENT RELATIONS, COMPETITION AND CONSUMERS

This document follows the consultation we issued in April on the Government's proposals for giving effect to Regulation 1/2003 and for re-aligning the Competition Act 1998. It forms part of our work to ensure that, following the "modernisation" of European competition law, our national competition authorities are acting consistently irrespective of whether they are applying the Chapter I or II prohibitions or Article 81 or 82, and to ensure that the Competition Act 1998 remains closely aligned to the EC system so that we fulfil this objective.

The aim, in 1998, of creating a domestic system, which mirrors that in Europe, was to minimise the burdens on business that working under two different systems would create. If we fail to re-align the Competition Act 1998 now that the European system is changing, we will risk imposing exactly the burden we were originally at pains to avoid. We want to create a UK competition regime that is truly world-class by combining the best of the existing system with the best of the new system.

The Competition Act 1998 has now been in force for three years but was actually drafted over five years ago. Major concerns then were to avoid excessive notifications and to provide a smooth transition from the Restrictive Trade Practices Act 1976 to the tougher prohibitions-based approach of the Competition Act 1998. Five years on, it is important to review whether the exclusions we introduced then still have a place in our domestic competition regime. Modernisation may have removed the value of some exclusions and some are likely to result in different treatment for agreements under the two systems of law. In principle, we should only remove sectors of the economy or classes of agreement from

the scope of competition law when there are compelling reasons to do so. Last year, in the Enterprise Act 2002, we removed a regime that offered special treatment to the professions for exactly this reason.

“Modernisation” is good news for businesses across Europe. It strengthens the position of our national competition authorities in ensuring that markets work fairly across Europe for the benefit of everyone and it ensures consistent treatment for agreements which affect trade between Member States, wherever those agreements are in operation. I believe it would be beneficial to business overall if we could extend that consistent treatment to agreements under our domestic law, so that companies are clear where they stand, whichever of the two systems they happen to be subject to.

The purpose of this consultation is to seek your views on whether some of the Competition Act 1998 exclusions that are currently in place should be removed to align the operation of European and domestic law.

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Purpose of this consultation

This consultation document seeks your views, in the context of the Government's proposals for giving effect to Regulation 1/2003 EC and for re-alignment of the Competition Act 1998, on whether certain exclusions and exemptions in the Competition Act 1998 should be repealed.

Responses

You can respond to this consultation:

by e-mail: competitionmodernisation@dti.gsi.gov.uk

by post: Nicholas Wortley
Consumer and Competition Policy Directorate
Room 608
Department of Trade and Industry
1 Victoria Street
London, SW1H 0ET
Telephone: 020 7215 6543

Closing date

Responses must be received by 12th August 2003.

Outcome

We aim to publish the outcome of this consultation by 30th September 2003.

Confidentiality

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 (including your identity) to be made public, you must state in the response which parts you wish us to keep confidential. Where confidentiality is not requested, responses may be made available to any enquirer, including enquirers outside the UK, or published by any means, including on the Internet. Please be aware that 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

We are sending this document to the consultees listed in Annex C. Please tell us if you know of others who would be interested in receiving this consultation. It is also available by request from the sources listed on our website, <http://www.dti.gov.uk/>.

Help with queries

If you would like help with queries or further information about this consultation please contact Kehinde.Macauley@dti.gsi.gov.uk,
Telephone: 020 7215 2174.

1. INTRODUCTION

1.1 On 1st April 2003, we published a consultation document on the Government's proposals for giving effect to Regulation 1/2003 EC ('the Regulation') and for re-aligning the Competition Act 1998 ('the Competition Act')¹. In that document we announced that we would publish a further consultation on our approach to exclusions and exemptions under the Competition Act following modernisation of competition law enforcement in Europe. This document outlines the Government's proposals on how exclusions and exemptions under the Competition Act should be treated after 1st May 2004 when the Regulation comes into force. In generating the proposals in this document, we have also completed the final stage of a review of the operation of the Competition Act, initiated in the White Paper "Productivity and Enterprise: A World Class Competition Regime" (July 2001) and partly implemented by the Enterprise Act 2002 ('the Enterprise Act').

1.2 The Regulation was approved by the European Council of Ministers in November 2002. It replaces Regulation 17/62, which establishes the Commission's powers, procedures and penalties for enforcing the EC Treaty Articles on competition (Articles 81 and 82²). The Regulation radically overhauls the framework of European competition law and has four main effects.

¹ UK Competition Law: Modernisation – a consultation on the Government's proposals for giving effect to Regulation 1/2003 EC and for re-alignment of the Competition Act 1998, April 2003, URN 03/750 available at

<http://www.dti.gov.uk/ccp/consultpdf/compmocon.pdf> and in hard copy by ordering from DTI Publications online at: <http://www.dti.gov.uk/publications/>

² Article 81 of the EC Treaty prohibits all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the Single Market. Article 82 prohibits any abuse by one or more undertakings of a dominant position within the Single Market or a substantial part of it insofar as such abuse may affect trade between Member States.

1.3 Firstly, it abolishes the system by which companies must notify an agreement to the Commission to obtain the legal certainty provided by an individual exemption under Article 81(3)³. It replaces this system with a “legal exception” regime in which agreements are either legal or illegal at the outset without requiring any prior administrative decision by the Commission⁴. Secondly, the Regulation sets minimum standards of competition enforcement, ensuring equal treatment of commercial agreements across Europe. It achieves this by:

- enabling national competition authorities (NCAs) and national courts to apply in full the Treaty Articles on competition;⁵
- requiring that Articles 81 and 82 be applied, in parallel to domestic competition law, to agreements or conduct that may affect trade between Member States; and
- requiring that decisions under national competition law about agreements must not reach a different outcome from the decision that would be reached under Article 81⁶.

1.4 Thirdly, the Regulation requires that Member States co-operate closely in enforcing competition law, enabling NCAs to exchange information and to conduct investigations on each other’s behalf. A European Competition Network (ECN) has been established to facilitate this process.

1.5 Finally, the Regulation strengthens and clarifies the Commission’s powers of investigation, widens the range of available remedies and provides tougher penalties for procedural infringements. Further detail on the implications of the Regulation for the operation of our existing

³ Where the agreement was appreciably restrictive of competition and would otherwise be prohibited by Article 81(1).

⁴ See section 3 of our earlier consultation document: for details see footnote 1.

⁵ Under Regulation 17/62, only the Commission can provide an exemption under Article 81(3).

⁶ Although note that the Regulation allows the application of stricter national laws regarding unilateral conduct.

national competition law can be found in our earlier consultation document⁷.

Implications for our domestic exclusions and exemptions

1.6 The Competition Act introduced a system of domestic competition law based on Articles 81 and 82. The express purpose of mirroring the EC system was to reduce the burdens on business of having to comply with two separate competition regimes. However, the changes to the EC regime resulting from the Regulation create a mis-alignment with the system of competition law established under the Competition Act. This will therefore increase the burden on business that basing the domestic regime on the EC regime was originally designed to relieve.

1.7 The Government believes that it is in the best interests of both business and the UK NCAs that the substantive law and the procedures of the UK NCAs are, as far as practicable, similar under both the Chapter I and II prohibitions and Articles 81 and 82. The proposals outlined in our earlier consultation document reflect this aim.

1.8 In addition, we believe it is also right to review the differences in scope between the two systems. Differences in scope arise primarily from two sources. Firstly, the Competition Act applies to agreements and conduct that may affect trade *within the UK* whereas the EC Treaty Articles on competition apply to agreements and conduct that affect trade *between Member States*. Secondly, agreements and conduct may be treated differently in the UK because they have been excluded from the scope of the Competition Act altogether.

⁷ See footnote 1.

1.9 Currently it is possible for an agreement or conduct to be excluded from our domestic competition law yet be caught by Article 81 or 82. This has been the case since the Competition Act was brought into force and has been emphasised in the Office of Fair Trading (OFT) guidelines⁸.

1.10 The Regulation does not alter this position. What it does do is to enable the OFT and the sectoral regulators⁹ to apply Articles 81 and 82 in full for the first time. It also provides that, where a NCA applies national competition law to agreements and conduct falling within Articles 81 and 82, it must also apply Articles 81 and 82. After modernisation, undertakings that benefit from a UK exclusion may nevertheless be subject to an examination of the same agreement or conduct by a UK NCA applying EC competition law. This will occur wherever the agreement or conduct may affect trade between Member States. The test of whether inter-state trade is affected has been given a wide interpretation by the European Court of Justice¹⁰ and many agreements made by UK companies are therefore likely to fall within Article 81.

1.11 If the two systems are not aligned, business would therefore have to assess which system applies (or if both apply) by deciding whether or not the agreement or conduct may affect trade between Member States. This would reduce legal certainty and create additional burdens on business. It would also be inconsistent for the same authority to treat the same type of agreement or conduct differently where the same assessment of anti-competitive effects applies and there is no differentiating factor other than an effect on trade between Member States. We therefore believe that the better regulatory approach is to

⁸ See for example Vertical Agreements and Restraints, OFT 419, March 2000, para 4.3

⁹ OFTEL (shortly to be incorporated into OFCOM), OFGEM, OFWAT, OFREG NI, ORR and CAA all have concurrent powers under the Competition Act.

¹⁰ The Commission intends to issue a draft notice on this topic in the Autumn.

minimise the differences between EC competition law and the Competition Act as far as practicable.

1.12 Some types of exclusions present more problems than others. There are four main categories:

Category 1 – exclusions from the Competition Act for agreements or conduct that are likely to have little or no effect on trade between Member States;

Category 2 – exclusions from the Competition Act for agreements or conduct where there could be an effect on trade between Member States but for which there is equivalent treatment in EC law;

Category 3 – exclusions from the Competition Act for agreements where there could be an effect on trade between Member States and for which the treatment in EC law differs in scope from our domestic exclusion;

Category 4 – exclusions from the Competition Act for agreements where there could be an effect on trade between Member States and for which there is no equivalent treatment in EC law.

1.13 Annex B contains a table detailing the exclusions from the Competition Act and the categories into which they may fall. Exclusion of agreements and conduct in categories 1 and 2 are of limited potential concern because there is little or no risk of any inconsistency in the treatment of these agreements or conduct by UK NCAs. Agreements falling within these categories include land agreements, planning obligations, agricultural products and merger situations¹¹. This

¹¹ Article 3(3) of Regulation 1/2003 provides an exception to the Regulation for situations in which NCAs and national courts of Member States apply national merger control laws.

consultation does not address the exclusions falling within categories 1 and 2. Nor does it address the UK block exemption on bus ticketing for the same reason¹².

1.14 Agreements or conduct falling within categories 3 and 4 are of potential concern and our domestic exclusions may need to be amended or removed to ensure consistent treatment under UK and EC law. These categories include vertical agreements, agreements given clearance under section 21(2) of the Restrictive Trade Practices Act 1976 and agreements which are subject to competition assessment via provisions in statutes other than the Competition Act, for example the rules and guidance issued by the recognised supervisory or qualifying bodies in the accountancy profession¹³.

1.15 Not all exclusions potentially falling into categories 3 and 4 are included in this consultation. Schedule 3 to the Competition Act contains two provisions enabling the Secretary of State to exclude any agreement or conduct from the application of the Chapter I or Chapter II prohibitions by Order in specified circumstances. Paragraph 6 of Schedule 3 enables the exclusion of conduct or agreements to avoid a conflict between the provisions of the Competition Act and an international obligation of the United Kingdom. Paragraph 7 of Schedule 3 enables the exclusion of conduct or agreements where there are "*exceptional and compelling reasons of public policy*" to do so. Neither of these powers to exclude agreements or conduct has been exercised thus far.

1.16 These powers to exclude were originally introduced for specific policy reasons, despite the lack of an EC equivalent. We have concluded

¹² The Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order 2001, SI 2001/319

¹³ Schedule 14 to the Companies Act 1989 and the Companies (Northern Ireland) Order 1990, SI 1990/593(NI5)

that the policy reasons for their introduction are still valid and that, in practice, they are unlikely to undermine the effective parallel enforcement of the two systems of competition law. In exercising these powers, the Secretary of State would have to consider the impact of the Regulation and her duties under Article 10 of the EC Treaty¹⁴. Any subsequent exclusion would therefore probably fall into category 1 or 2 and would not be of concern.

1.17 We do not address the exclusions from the Competition Act for the rules of the FSA and for recognised investment exchanges and clearing houses¹⁵ or the related exclusion for EEA regulated markets¹⁶. The Government committed to reviewing the impact of the Financial Services and Markets Act 2000 on competition in financial services markets, two years after it came into force in December 2001, in its response of August 2000 to the Cruickshank Report on competition in UK banking. The Government is already considering its response to this commitment. Nor do we consider the exclusions for Channel 3 news provision and networking agreements¹⁷. The Government amended the Broadcasting Act 1990 in the Communications Bill to provide powers for OFCOM to scrutinise the Channel 3 networking agreements under both Chapter I and Article 81 EC and the exclusions and their corresponding scrutiny regimes will fall in their entirety to OFCOM under its competition powers. There is therefore no need to consider them further here.

¹⁴ Article 10 of the Treaty establishing the European Community states that "Member States shall take all appropriate measures, whether general or particular, to ensure fulfilment of the obligations arising out of this Treaty or resulting from action taken by the institutions of the Community. They shall facilitate the achievement of the Community's tasks. They shall abstain from any measure which could jeopardise the attainment of the objectives of this Treaty"

¹⁵ See Part I of Schedule 2 to the Competition Act

¹⁶ See para 3 of Schedule 3 to the Competition Act

¹⁷ See Part III of Schedule 2 to the Competition Act

Next steps

1.18 Following responses to this consultation and to our parallel consultation on giving effect to the Regulation and aligning the Competition Act, the Government intends to draft a Statutory Instrument, which will amend the Competition Act. We expect to publish this Statutory Instrument in draft in Autumn 2003 and to bring it into force on 1st May 2004 to coincide with the coming into force of the Regulation. The Statutory Instrument will be made under powers in section 2 of the European Communities Act 1972 and the express power to align the Competition Act in section 209 of the Enterprise Act.

1.19 The OFT will update existing Competition Act guidelines as well as the Director's Rules¹⁸ to include any changes arising from modernisation and will produce a modernisation guideline, expected to be published for consultation in the Autumn.

References to the OFT

1.20 Readers should note that, whilst this document refers to the OFT throughout, where a reference to the powers of the OFT is made, such a reference should be read as referring equally to all the regulators with concurrent competition powers. These include OFTEL (shortly to be incorporated into OFCOM), OFGEM, OFWAT, OFREG NI, ORR and CAA.

The Government welcomes views on the questions asked in this document and any information that would inform the development of the partial RIA at Annex D.

¹⁸ Competition Act 1998 (Director's rules) Order 2000, SI 2000/261

2. SUMMARY OF QUESTIONS FOR CONSULTATION

- Consequent to its proposal to remove the domestic notification system and to create a legal exception regime in the UK, the Government also proposes to remove the power in section 7 of the Competition Act to introduce opposition procedures into Block Exemption Orders. The Government seeks views on its proposal.
- The Government proposes to remove the Exclusion Order for vertical agreements under the Competition Act and seeks views on the likely impact of this proposal.
- The Government seeks information on the number and types of UK vertical agreements, which will now be open to competition scrutiny as a result of removing the Exclusion Order (whilst retaining the Block Exemption Regulation applicable under section 10 of the Competition Act) and which are not already subject to the Chapter II prohibition. The Government also seeks information on the likely costs of further legal consideration of these agreements. This information will help to inform the Regulatory Impact Assessment at Annex D.
- The Government proposes to repeal the separate competition scrutiny regime for statutory audit services and consequential exclusion from the Competition Act. We would welcome your views on this proposal.
- The Government proposes to repeal the provisions of the Environment Act that allow for the creation of a separate competition scrutiny regime for Producer Responsibility Schemes

and for the exclusion of such schemes from the Competition Act.
We welcome your views on this proposal.

- The Government seeks your views on whether to remove the exclusion from the Competition Act for agreements given clearance under section 21(2) of the Restrictive Trade Practices Act 1976, and on the number of agreements that might be affected if the exclusion were to be removed.

3. BLOCK EXEMPTIONS

3.1 The most fundamental change to European competition law arising from the Regulation is the abolition of the system of notifications established by Regulation 17/62 and the creation of a system based on the principle of “legal exception”. The changes to the EC system and the implications for the operation of our domestic notification system are discussed in detail in section 3 of our consultation on the Government’s proposals for giving effect to the Regulation¹⁹. In that consultation document, we propose that the domestic system of notifications should be removed in line with the EC system and a legal exception regime created under the Competition Act. The reader is referred to the earlier consultation document for further details on this proposal.

3.2 The removal of the notification system will affect how EC Block Exemption Regulations (BERs) and UK Block Exemption Orders (BEOs) made under the Competition Act work. This section discusses how the Regulation affects BERs and the implications for our domestic law.

The effect of the Regulation at EC level

3.3 BERs are designed to provide “safe harbours” for specified categories of agreement where they meet the exemption criteria in Article 81(3)²⁰. They are generally made by the Commission, acting under

¹⁹ See footnote 1.

²⁰ Article 81(3) exempts any agreement, decision or concerted practice “which contributes to improving the production or distribution of goods or to promoting technical or economic progress, whilst allowing consumers a fair share of the resulting benefit, and which does not – (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives; and (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question”

powers granted by regulations of the Council of Ministers²¹. Agreements falling within the terms of a BER are already legal and do not require prior notification to the Commission. To benefit from a BER, an agreement must satisfy all its requirements. Where the agreement fails to do so, a notification can still be made for individual exemption.

3.4 The Commission has been aware for some years that the existing process of seeking individual exemption through notification is administratively inefficient and has long since ceased to function optimally either for business or for the Commission itself. Early BERs were also highly prescriptive which increased the need to notify agreements falling marginally outside their scope. The Commission addressed these issues initially by including a “fast-track” exemption procedure known as an “opposition procedure” in certain BERs²². An opposition procedure typically requires the undertaking to notify its agreement to the Commission in the usual way and enables the Commission to oppose the notification within a specified period²³. The Commission may publish details of the application and invite comments. If no serious objections are raised, the agreement is deemed to be exempt.

3.5 In practice, these “fast-track” procedures have been little used and where they have, agreements have often failed to obtain exemption. In addition, the Commission has tried to make its more recent BERs less prescriptive by including only “blacklisted” provisions rather than a corresponding “white” or “grey” list of permissible provisions, as in its early BERs. Only one recent BER has contained an opposition procedure;

²¹ The Council has, on occasion, granted Block Exemptions itself, for example 1017/68/EEC Council Regulation applying rules of competition to transport by rail, road and inland waterways

²² Article 12 of 1017/68/EEC

²³ For example, the period specified is 90 days in the case of Council Regulation 1017/68/EEC

Regulation 240/96 on technology transfer agreements, and the procedure has therefore gradually fallen out of favour.

3.6 With the removal of notifications under modernisation, the remaining opposition procedures in BERs will also be removed. The opposition procedures in Council Regulation 1017/68²⁴ (regulation relating to transport by road, rail and inland waterways) and Council Regulation 4056/86²⁵ (a block exemption for certain liner conferences) will be repealed by Articles 36 and 38 respectively of the Regulation and the Commission intends to remove opposition procedures in other BERs wherever they exist.

Implications for the current UK system

3.7 The Competition Act contains provisions enabling the Secretary of State (on the recommendation of the OFT) to exempt categories of agreement from the Chapter I prohibition in much the same way as the Commission. Section 7 of the Competition Act provides that a Block Exemption Order (BEO) *may* include an opposition procedure. Under such a procedure, a party to an agreement which does not qualify for the block exemption created by the Order, but which satisfies specified criteria, can notify the agreement to the OFT. If at the end of a specified period, the OFT does not notify the party of its opposition to the agreement, the agreement is treated as falling within the Block Exemption Order.

3.8 Only one BEO has been made under the Competition Act to date; the Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order 2001. This BEO exempts public transport ticketing schemes, which meet the detailed conditions of the BEO, from the

²⁴ 1017/68/EEC Council Regulation applying rules of competition to transport by rail, road and inland waterway

²⁵ 4056/86/EEC Council regulation laying down detailed rules for the application of Articles 85 and 86 of the Treaty to maritime transport

Chapter I prohibition. Public transport ticketing schemes are written agreements between suppliers of local public transport services (in one case together with long distance public transport operators) to provide tickets and travel cards enabling travel on the services of more than one supplier. However, the Public Transport Ticketing Schemes BEO does not contain an opposition procedure because the terms of the BEO were highly specific and, in light of this, an opposition procedure was unnecessary.

3.9 The Government intends to retain powers in the Competition Act²⁶ to provide for BEOs since it is likely that, in future, there will be instances in which it is desirable to exempt categories of agreements (such as transport ticketing schemes) from domestic competition law. Clearly the scope of any such future BEOs would take into account the impact any provisions of the Regulation may have.

3.10 The Government is currently consulting on its proposal to remove the domestic notification system and to create a legal exception regime under the Competition Act. Under a legal exception regime, agreements, decisions and concerted practices that are caught by the Chapter I prohibition in section 2 and *do not* satisfy the criteria in section 9 of the Competition Act²⁷ will be illegal at the outset. Agreements, decisions and concerted practices that are caught by the Chapter I prohibition in section 2 but which *satisfy* the criteria in section 9 of the Competition Act will be valid and fully enforceable at the outset. It will be for the party alleging

²⁶ See sections 6 and 8 of the Competition Act.

²⁷ Section 9 of the Competition Act outlines the criteria for individual and block exemptions. It applies to any agreement which-

- (a) contributes to (i) improving production or distribution, or (ii) promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit; but
- (b) does not (i) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; or (ii) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

the infringement (a UK NCA or a private litigant) to prove an infringement of Chapter I and for the party claiming the benefit of section 9 to prove that the conditions of that section are met. Undertakings will make their own assessments of the legality or otherwise of their agreements, as the majority do now.

3.11 In this context, the provision in section 7 of the Competition Act providing for an opposition procedure based on notification will need to be removed. An undertaking will make its own assessment of whether or not its agreement falls within the terms of a BEO. Given that the inclusion of an opposition procedure in BEOs is a discretionary power and that the single BEO currently in operation under the Competition Act does not contain such a procedure, the Government's view is that the likely impact of removing section 7 will be minimal.

Consequent to its proposal to remove the domestic notification system and to create a legal exception regime in the UK, the Government also proposes to remove the power in section 7 of the Competition Act to introduce opposition procedures into Block Exemption Orders. The Government seeks views on its proposal.

4. VERTICAL AGREEMENTS

4.1 A vertical agreement is an agreement between two or more parties, each of which operates at a different stage in the supply chain. These agreements can be at any level of the supply chain. For example, they may be between manufacturers and wholesalers or retailers, wholesalers and retailers, retailers and customers or even between two wholesalers provided they are operating at different levels of the supply chain for the purposes of the agreement. Typical vertical agreements include distribution agreements, purchasing agreements, selective distribution agreements and franchise agreements.

4.2 In its White Paper “Productivity and Enterprise: A World Class Competition Regime”, the Government signalled its intention to repeal the domestic exclusion from the Competition Act for vertical agreements²⁸. In light of the detail of the White Paper responses and also given that the precise terms of the modernisation of EC competition law were still unclear, the Government decided to consider the proposal further once negotiations on the Regulation had been concluded. This section outlines the current position in relation to vertical agreements and discusses how they should be treated when the Regulation comes into force.

Vertical agreements under the UK regime

4.3 Most vertical agreements are excluded from the Chapter I prohibition of the Competition Act by the Competition Act 1998 (Land and Vertical Agreements Exclusion) Order 2000 (‘the Exclusion Order’)²⁹. The Exclusion Order provides that “the Chapter I prohibition shall not

²⁸ July 2001 White Paper, Productivity and Enterprise – A World Class Competition Regime, sections 8.14 to 8.16

²⁹ S.I. 2000/310 made under section 50 of the Competition Act

apply to an agreement to the extent that it is a vertical agreement”³⁰. Article 2 of the Exclusion Order defines a vertical agreement as “an agreement between undertakings, each of which operates, for the purposes of the agreement, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services and includes provisions contained in such agreements which relate to the assignment to the buyer or use by the buyer of intellectual property rights, provided that those provisions do not constitute the primary object of the agreement and are directly related to the use, sale or resale of goods or services by the buyer or its customers.”

4.4 The exclusion is automatic and no individual notification needs to be made to the OFT to benefit from its provisions. Further guidance about how this exclusion operates can be found in the OFT’s guidelines “Vertical Agreements and Restraints”³¹ and “Assessment of Individual Agreements and Conduct”³².

4.5 The Exclusion Order came into force on 1 March 2000, at the same time as the Competition Act. One of its aims was to reduce the burden on business of making precautionary notifications under the Competition Act of large numbers of essentially benign agreements, and to allow the competition authorities to concentrate their resources on matters of significant competition concern, rather than on the detailed scrutiny of such agreements.

4.6 Responses to the earlier consultation suggest that the Exclusion Order has been perceived as providing a blanket protection from competition scrutiny for vertical agreements. It was never intended that

³⁰ Article 3 of the Exclusion Order

³¹ Vertical Agreements and Restraints, OFT 419, March 2000

³² Assessment of Individual Agreements and Conduct, OFT 414, September 1999

the Exclusion Order should provide this degree of protection nor is that the actual legal effect of its terms. The protection offered by the Exclusion Order is limited in a number of ways under UK competition law.

4.7 Firstly, *the Exclusion Order applies to an agreement only to the extent that it is a vertical agreement*. Agreements that contain provisions concerning matters other than the vertical agreement will therefore benefit from the Exclusion Order only in part.

4.8 Secondly, *the Exclusion Order does not apply to agreements that fix prices*. Article 4 of the Order provides that the exclusion for vertical agreements does not apply to any vertical agreement that, directly or indirectly, has the object or effect of restricting the buyer's ability to determine its sale price. Agreements where the supplier imposes a maximum or recommended sale price may benefit from the Exclusion Order except where these result, in practice, in a fixed or minimum sale price because of pressure from, or any incentives offered by, any of the undertakings involved³³.

4.9 Thirdly, *the OFT can terminate ("claw back") the benefit of the exclusion for a particular agreement* where, for example, it considers that the agreement would infringe the Chapter I prohibition but for the Exclusion Order and would not merit an unconditional individual exemption³⁴.

4.10 Lastly, *the Exclusion Order does not exclude vertical agreements from the application of any provisions of UK competition law other than the Chapter I prohibition*. Vertical agreements can still be considered as part of the conduct of an undertaking under the Chapter II prohibition.

³³ For further detail see paragraphs 3.1 to 3.3 of Vertical Agreements and Restraints, OFT 419, March 2000

³⁴ Article 7 of the Exclusion Order.

An undertaking may fall within Chapter II of the Competition Act if it has a dominant position on the relevant product market. The OFT considers it unlikely that an undertaking will be individually dominant if its market share is below 40%³⁵. In addition, the complex monopoly provisions of the Fair Trading Act 1973 (and shortly the Market Investigation provisions of the Enterprise Act) may be applied where the structure of a market raises competition concerns and vertical agreements can be considered where relevant in this context.

Vertical agreements under the EC regime

4.11 Even though a vertical agreement may benefit from the Exclusion Order, the domestic exclusion cannot affect the application of the EC Treaty Articles in any case where the agreement may also affect trade between Member States. However, since the Exclusion Order was made, the Commission has also introduced a Block Exemption for vertical agreements³⁶. This Block Exemption Regulation (BER) provides a “safe harbour” for large numbers of vertical agreements under Article 81(3) and has parallel effect in the UK under section 10 of the Competition Act³⁷. Vertical agreements, which have an effect on trade within the UK or between Member States, can therefore rely on the provisions of the BER to exempt them from both the UK and EC prohibitions.

4.12 The Exclusion Order and the BER are similar in some respects. Both define vertical agreements in the same way, contain an exception for the ‘hardcore’ restriction of price fixing and include a “claw back” provision.

³⁵ For further detail see paragraphs 3.9 to 3.21 of The Chapter II Prohibition, OFT 402, March 1999.

³⁶ Commission Regulation 2790/1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, which came into force on 1st June 2000.

³⁷ Section 10 provides that “an agreement is exempt from the Chapter I prohibition if it does not affect trade between Member States but otherwise falls within a category of agreements which is exempt from the Community prohibition by virtue of a Regulation.”

Furthermore, the OFT, in its guideline "Vertical Agreements and Restraints" states that "*The exclusion from the Chapter I prohibition for vertical agreements provided in the Exclusion Order is intended to follow closely the treatment of vertical agreements in the European Community so that the burden on business of operating under different systems is minimised*"³⁸.

4.13 Broadly, the main differences between the Exclusion Order and the BER are that the BER applies subject to the relevant party³⁹ having a share below 30% of the relevant market and subject to the agreement not containing certain defined "hardcore" restrictions or other conditions. The Exclusion Order, by contrast, has no explicit market share test (although agreements between parties with some degree of market power are precisely those which could face "claw back" under the Exclusion Order as well as potentially falling within the Chapter II prohibition).

4.14 The BER will also not apply to agreements that contain one of the hardcore restrictions listed in Article 4. These include:

- **Resale price maintenance** – a supplier is not to fix directly or indirectly the price at which distributors can resell his products. However, a maximum resale price or a recommended resale price is not normally prohibited.
- **Restrictions concerning the territory into which or the customers to whom the buyer may sell** – as a general principle a distributor must remain free to decide where and to whom he sells and this cannot

³⁸ Vertical Agreements and Restraints, OFT 419, March 2000, para 4.4

³⁹ It is usually the supplier, except where agreements contain exclusive supply obligations, in which case it is the market share of the buyer that is considered.

be restricted by the agreement. This general principle is subject to certain exceptions⁴⁰.

- **Restrictions on the sales to end-users by authorized distributors in a selective distribution network** – a producer applying a selective distribution system cannot restrict active or passive selling by the authorised distributors to end-users, except that the supplier can require the distributor to sell only from a given location.
- **Restrictions on authorised distributors in a selective distribution network selling or purchasing from other members of the network** – the appointed distributors in a selected distribution system cannot be restricted from buying or selling the contract goods to or from other appointed distributors within the network.
- **Restrictions preventing the sale of components as spare parts by the manufacturer of the component to end-users, independent repairers and service providers** – an agreement between a manufacturer of component parts and a buyer which incorporates these parts into its own products (the original equipment manufacturer) may not prevent or restrict sales by the manufacturer of these component parts as spare parts to end users, independent repairers or service providers.

4.15 Article 5 of the BER also imposes specific conditions for non-compete obligations during the contract, non-compete obligations after the termination of the contract and the exclusion of specific brands in a

⁴⁰ The supplier can restrict a buyer from making “active sales” into a territory allocated to another buyer or which the supplier has reserved to itself, the supplier can restrict sales by a wholesaler to end-users, the supplier can restrict distributors in a selective distribution network from selling to unauthorized distributors and the supplier can restrict a buyer of components supplied for incorporation from reselling them to competitors of the supplier. Article 4(b) of EC Commission Regulation 2790/99

selective distribution agreement. When the conditions are not fulfilled, these vertical restraints are excluded from the exemption, although the BER continues to apply to the rest of the vertical agreement if that part is severable from the non-exempted vertical restraints.

The effects of the Regulation

4.16 After the new Regulation comes into force, both Article 81 and the Chapter I prohibition will be applied by OFT and where relevant the sectoral regulators. Article 3 of the Regulation sets out the relationship between EC and national competition law and requires that wherever the NCAs and national courts in Member States apply national competition law to agreements or conduct within the scope of Article 81(1) or Article 82, they *must* also apply Article 81 or 82. After 1st May 2004, the enforcement of the Competition Act will therefore be taking place in the same institutional framework as the enforcement of Articles 81 and 82 and greater emphasis will inevitably fall on whether an agreement has an effect on trade between Member States. Both business and UK NCAs will need to consider whether the Exclusion Order or the BER (including by parallel operation), or both, apply to a vertical agreement.

4.17 In introducing the Competition Act and the Enterprise Act, one of the Government's main aims has been to provide a domestic regime that reflects the operation of the competition regime in Europe, thus minimising the burden on business of operating two different systems. The Government believes that it is preferable to reduce as far as possible any substantive and procedural differences between the Competition Act and EC competition law created by the introduction of the new Regulation. This approach has informed the Government's recent consultation on other aspects of modernisation and the approach to exclusions discussed elsewhere in this document. Ideally, there should be

no significant difference between the result of applying Articles 81 and 82 or the Competition Act.

4.18 At present, both the BER (by parallel operation) and the Exclusion Order apply to agreements under the Chapter I prohibition. The Government believes that this position is undesirable and should be resolved as it is potentially confusing for business. The requirement for NCAs to apply Article 81 in parallel to domestic law following the Regulation is likely to cause greater confusion in practice, as the two regimes may need to be considered by the same NCA in relation to the same agreement or conduct. In view of this, the Government believes that the better regulatory approach is to repeal the Exclusion Order and rely on the BER.

The rationale for relying on the BER (by parallel operation)

4.19 When the Government was considering the Exclusion Order, the treatment of vertical agreements in EC law was under review and the Government acknowledged that this was a reason to be cautious about introducing a domestic exclusion. Responses to our consultation in 1999 led us to conclude that it would be desirable to have an exclusion in place when the Competition Act came into force to avoid numerous precautionary notifications of benign agreements. When the draft statutory instrument was in preparation, the BER was still being negotiated and had not been agreed by the Council of Ministers. Once agreed, it did not then take effect until June 2000, three months after the coming into force of the Competition Act. The Government recognised the need to keep the operation of the Exclusion Order under review in the light of experience. The Exclusion Order was given effect by secondary legislation so as to provide the necessary degree of flexibility.

4.20 The Competition Act has been in force for three years and it is right that we now review whether the Exclusion Order should remain in place. In the Government's view it should not.

4.21 In our previous consultation in 1999, the Government stated that *"economic analysis suggests that vertical agreements do not generally give rise to competition concerns unless one of the parties to the agreement has significant market power or there exists a large network of similar agreements. Although they may restrict competition from retailers selling the same brand ("intra-brand competition"), vertical agreements can also work to stimulate competition between brands ("inter-brand competition") and can provide wider benefits"*⁴¹.

4.22 The BER was drafted to reflect the link between market power and the potential for vertical agreements to give rise to competition concerns. Many vertical agreements are presumed to be legal but where the relevant party has a market share of 30% or more, the agreements can be reviewed under Article 81 as well as Article 82. It also identifies the "hardcore" restrictions, which are more likely to cause concern and are therefore subject to individual scrutiny. It therefore more precisely reflects agreed economic analysis across the EU of the effects of vertical agreements.

4.23 The removal of the Exclusion Order will not affect the application of Articles 81 and 82 to vertical agreements in the UK which also affect trade between Member States. These agreements may be considered within the EC regime if they restrict competition and may or may not benefit from the BER. Nor does removing the Exclusion Order affect those

⁴¹ Competition Act 1998 Exclusion of Vertical Agreements: Consultation on a draft Order, February 1999 (URN 98/1030), paragraph 5

agreements that may affect trade only within the UK and which fall within the BER as a parallel exemption.

4.24 Broadly, the agreements principally affected by repealing the Exclusion Order are those where:

- the supplier or buyer is not dominant (see paragraph 4.10 above);
and
- there is no effect on trade between Member States, so that only the Chapter I prohibition would apply; and
- the BER by parallel operation does not apply. This would be the case only where one of the following factors existed:
 - the supplier/buyer (depending on the circumstances) has a market share of more than 30%; or
 - the agreement involves one of the hard-core restrictions (other than Resale Price Maintenance) set out in Article 4 of the BER;
or
 - the agreement contains a non-compete clause which runs for more than 5 years during the course of an agreement or for more than one year after the termination of the agreement; or
 - the agreement is a selective distribution agreement which contains restrictions on the distributor selling particular competing brands.

4.25 Even where a vertical agreement with no effect on trade between Member States clearly falls outside the terms of the BER, it must still be appreciably restrictive of competition to fall within the scope of the Chapter I prohibition. The Chapter I prohibition applies only where the object or effect of the agreement is to prevent, restrict or distort competition within the UK. The OFT assesses whether the effect of an agreement on competition is appreciable by examining its market and economic context. This includes the content of the agreement and the

structure of the market or markets affected such as the entry conditions, the characteristics of buyers and the structure of the buyers' market. At present, an agreement is unlikely to have an appreciable effect on competition unless the parties' combined share of the relevant market exceeds 25%⁴². However even where the parties' combined market share exceeds 25%, the OFT may still find that the effect on competition is not appreciable⁴³. Those agreements, which are genuinely benign in effect, will not be caught by the Competition Act and are already entirely legal.

4.26 The table at Annex A provides an overall comparison of the two regimes and may help to show which agreements (if any) would be affected by the removal of the Exclusion Order.

The Government seeks information on the numbers of agreements falling within the above description and the likely costs of further legal consideration of these agreements. This information will help to inform the Regulatory Impact Assessment at Annex D.

4.25 The Government believes that the Order excluding vertical agreements from the Competition Act should be repealed, leaving the BER in place as a parallel exemption⁴⁴. Repeal of the Exclusion Order ensures maximum visible correspondence between the UK and EC regimes. It also reflects growing business understanding of the regime and our confidence in the UK's independent competition authorities to apply both the Competition Act and Community law in a sensible and proportionate way. It also removes the requirement to determine which applies to a given agreement. The BER retains a "safe harbour" for many vertical

⁴² Combined market shares are relevant only to the extent that the parties operate in the same relevant market. Where none of the parties' operations concern the same level of the supply chain, their operations would not overlap in the same relevant market.

⁴³ Further information on the "appreciable effect" test and assessment of market power can be found in: Assessment of Market Power, OFT 415, September 1999

⁴⁴ This would not affect those provisions relating to land agreements.

agreements whilst opening up to scrutiny exactly those agreements that are appreciably restrictive of competition and where, because of the exercise of market power, there may be reason to be concerned.

The Government proposes to remove the Exclusion Order and seeks views on the likely impact of this proposal.

5. COMPETITION SCRUTINY REGIMES

5.1 The Restrictive Trade Practices Act 1976 (RTPA) contained a number of exclusions for agreements and practices that were subject to separate competition scrutiny regimes in other legislation. When the Competition Bill was before Parliament, it was decided that some of these exclusions should be continued to allow a smoother transition for the parties affected between the old and the new regime. One such exclusion in Schedule 2 to the Competition Act, is for the rules and guidance of supervisory and qualifying bodies for statutory audit “recognised” under the Companies Act 1989 (‘the Companies Act’)⁴⁵.

5.2 Schedule 2 to the Competition Act also contains a power to exclude Producer Responsibility Obligations made under the Environment Act 1995 (‘the Environment Act’) from the Chapter I and II prohibitions. The corresponding scrutiny regime, which was first introduced in 1997 was repealed two years later⁴⁶.

5.3 This section discusses the impact of the Regulation on competition scrutiny regimes and our approach to the exclusions in the Competition Act for Statutory Audit and Producer Responsibility Obligations⁴⁷.

⁴⁵ Part II to Schedule 2 of the Competition Act 1998 which amended Schedule 14 to the Companies Act 1989.

⁴⁶ The Producer Responsibility Obligations (Packaging Waste) Regulations 1997 SI 1997/648 and the Producer Responsibility Obligations (Packaging Waste)(Amendment)(No. 2) Regulations 1999,SI 1999/3447, which repealed regulations 31-33 of the previous Regulations.

⁴⁷ Information on the Government’s approach to other scrutiny regimes and the corresponding exclusions from the Competition Act can be found in paragraph 1.17 of the introduction to this document.

The Impact of the Regulation

5.4 As we discuss elsewhere in this paper and in our earlier consultation⁴⁸, one of the effects of the Regulation is that the OFT will be able to apply Article 81 and Article 82 directly, as well as the Competition Act. Under Article 3 of the Regulation, where a NCA applies national competition law to any agreement or conduct that may affect trade between Member States, it must also apply Article 81 or 82 to that agreement or conduct. Where national competition law is applied in parallel to Article 81, a NCA cannot reach a decision under national law which would be different from that which would be envisaged under EC law. Article 3 also provides that NCAs are not required to apply Article 81 or 82 in parallel when applying provisions of national law which predominantly pursue an objective different from that pursued by the Treaty Articles. The primary aim of Article 3 is to ensure minimum standards of competition enforcement under EC law across the European Union.

5.5 Article 3 will have important practical consequences for competition scrutiny regimes. The OFT may be required to apply Article 81 or 82 to UK agreements or conduct that may affect trade between Member States *even if it is barred from doing so under the Competition Act because an agreement is subject to an exclusion*. If an agreement or conduct does fall within the scope of the Treaty Articles, the domestic exclusion is no longer of any value. The UK authorities are already obliged to have regard to Article 10 of the EC Treaty when exercising competition scrutiny. However, there is also a risk that OFT might be regarded, albeit wrongly, as having given competition “clearance” to an agreement or conduct under a competition scrutiny regime. The tests in the scrutiny regimes do not demand the same level of competition

⁴⁸ See footnote 1.

scrutiny as that required by the Competition Act or the Treaty Articles⁴⁹ and are applied before the Regulation has been put into practice (ex ante) rather than once its effects are known (ex post). In future, OFT may in practice, have to apply a stricter level of scrutiny than it would have done previously under the competition test in the relevant statute.

5.6 There is no requirement in the Regulation to remove these domestic competition scrutiny regimes. Their purpose is essentially pro-competitive in that they are designed to prevent regulation having a more restrictive effect than is strictly necessary to achieve the regulatory aims. However, the obligations created by the Regulation are likely to place some constraints on the effective operation of these regimes where the agreements concerned may affect trade between Member States and where they cannot be clearly defined as state measures that do not fall to be examined under the EC Treaty Articles. These constraints will be most evident where the scrutiny is split between different regulators as OFT might be required to suspend the scrutiny applied under a separate competition test whilst it applies Article 81 or 82.

Competition Scrutiny of Statutory Audit

5.7 Under the Companies Act⁵⁰, the Secretary of State has powers to formally “recognise” accountancy bodies authorised to ensure the proper training of registered auditors (Recognised Qualifying Bodies or RQBs)⁵¹ and ensure the appropriate supervision of audit firms (Recognised

⁴⁹ Paragraph 1(2) of Schedule 14 to the Companies Act 1989 requires OFT to “consider whether the rules or guidance have or are intended or likely to have, to any significant extent the effect of restricting, distorting or preventing competition”. Section 95(2)(a) of the Financial Services and Markets Act 2000 requires OFT to consider whether “regulating provisions or practices have a significantly adverse effect on competition”.

⁵⁰ Also under the Companies (Northern Ireland) Order 1990 SI 1990/593 (NI 5)

⁵¹ RQBs are Association of Chartered Certified Accountants, Institute of Chartered Accountants in England and Wales, Institute of Chartered Accountants in Ireland, Institute of Chartered Accountants in Scotland, Association of International Accountants.

Supervisory Bodies or RSBs)⁵². The Companies Act also provides for the Secretary of State to seek competition advice from the OFT before deciding whether to recognise a RSB or a RQB. The OFT is required to advise on whether “the rules or guidance have or are intended or likely to have, to any significant extent, the effect of restricting, distorting or preventing competition”⁵³. The OFT is also required to keep the competition effects of the rules, guidance and practices of the bodies under review and advise the Secretary of State if there are competition concerns. There is a corresponding exclusion from the Chapter I prohibition of the Competition Act for agreements or practices scrutinised under the separate regime in the Companies Act⁵⁴.

5.8 In considering the effect of the Regulation on this regime, the Government has reviewed the relevant case law of the European Court of Justice (‘ECJ’). European case-law on the status, under competition law, of regulation which is delegated to non-Government bodies is not entirely clear and there have been no cases which precisely mirror the current position of the RQBs and RSBs.

5.9 However, the Government’s preliminary view is that the rules and guidance of the RSBs and RQBs may fall within the scope of the Treaty Articles on competition. The ECJ has adopted a broad interpretation of the types of agreements, decisions, concerted practices or conduct which may have an effect on inter-state trade and therefore fall within the scope of the EC Treaty Articles on competition. Case-law suggests that where an agreement, decision or concerted practice extends over the whole of the territory of a Member State (as for example with the rules of a professional body), it has, by its very nature, the effect of reinforcing the

⁵² RSBs are as above with the exception of Association of International Accountants but including Association of Authorised Public Accountants.

⁵³ Paragraph 1(2) of Schedule 14 to the Companies Act

⁵⁴ Paragraph 9, Schedule 14 to the Companies Act as amended by Part II of Schedule 2 to the Competition Act

compartmentalisation of markets on a national basis, thereby holding up the economic inter-penetration which the Treaty is designed to bring about. Such agreements or practices can be caught by Article 81⁵⁵.

5.10 In previous judgements, the ECJ has repeatedly held that professional associations are capable of falling within the definition of an “association of undertakings”⁵⁶ and that, even where such bodies are carrying out functions delegated to them under public law, the legal framework under which they are carrying out their regulatory functions will not necessarily preclude application of the Treaty Articles⁵⁷.

5.11 It is not necessarily the case that the rules and guidance of the RQBs and RSBs would be considered to be appreciably restrictive of competition. Nor is it clear that, even if they were considered to be appreciably restrictive, they would be prohibited under Article 81(1) or would not be exempt under Article 81(3). However, if OFT is required under the Regulation to consider the rules and guidance under EC law rather than UK law, the existing scrutiny regime and the corresponding exclusion from the Competition Act will be of more limited value after 1st May 2004.

5.12 It is also worth noting that Parliament has repealed Schedule 4 to the Competition Act in the Enterprise Bill and thus removed the special treatment available for the rules of professional bodies listed in the Schedule, including those of accountants. It is consistent with the Government’s general approach to the professions that the competition scrutiny regime in the Companies Act should now be removed and the

⁵⁵ See for example *Wouters, Savelberghand, Price Waterhouse Belastingadviseurs BV v Algeme Raad van de Nederlandse Orde van Advocaten*, Case C-309/99, paragraph 95

⁵⁶ See for example the *Wouters* case and *Pavel Pavlov v Stichting Pensioenfonds Medische Specialisten*, Case C-180 to 184/98[2000] ECR-16451

⁵⁷ *BNIC v Clair*, Case C123/83[1985] ECR391 and *CNSD v Commission*, Case T-513/93

rules and guidance of RQBs and RSBs brought fully within the scope of competition law.

The Government proposes to repeal the separate competition scrutiny regime for statutory audit services and consequential exclusion from the Competition Act. We would welcome your views on this proposal.

5.13 In considering these issues, it is also important to take into account other changes in the regulatory regime for auditors that are currently the subject of separate consultation. Following the high-profile collapses of Enron, WorldCom and Arthur Andersen, the Secretary of State announced on 29th January 2003 proposals to strengthen the regulatory regime for auditors. Among these was the assumption by the Financial Reporting Council (FRC) of the functions of the Accountancy Foundation to create a single, independent UK regulator. In March 2003, the Government issued a consultation document setting out proposals for the statutory framework within which the new FRC should operate⁵⁸. The consultation proposes, among other things, that the Secretary of State's powers to recognise RSBs and RQBs should be delegated to a statutory body established by the Secretary of State by a delegation order under section 46 of the Companies Act.

5.14 In practice, this delegated body would be identical to the Professional Oversight Board (POB), one of the five Boards of the new FRC. In *legal* terms, however, it would be a distinct entity from the POB, which would carry out certain day-to-day non-statutory functions, including the independent oversight and monitoring of the activities of the professional accountancy bodies. The Government's view is that the FRC, the POB, the RQBs and the RSBs may all fall within the definition of

⁵⁸ Review of the Regulatory Regime of the Accountancy Professions: Legislative Proposals, URN 03/717, available at <http://www.dti.gov.uk/cld/accountreg.pdf>

either an 'undertaking' or an 'association of undertakings' under competition law and any rules, guidance or practices, which cover the whole of the profession, could be within the scope of Articles 81 or 82.

5.15 In this scenario, retaining the scrutiny regime in the Companies Act would also have the effect of providing a form of notification for the RSBs and RQBs. Currently, under the Competition Act, undertakings can notify their agreements to the OFT for either formal guidance or a decision as to whether the agreements are caught by the Competition Act or would be prohibited under Chapter I or would benefit from an exemption under section 9 of the Competition Act⁵⁹. If the Secretary of State's powers to seek competition advice from OFT are also delegated to the POB alongside her powers to recognise the relevant bodies, the RQBs and RSBs would be able to benefit from a similar type of "clearance". However, the Government is currently consulting on its proposal to remove the notification regime under the Competition Act and to create a legal exception regime under which agreements are either legal or illegal at the outset, no prior administrative decision to that effect being required⁶⁰. It would therefore be consistent with this proposal to remove the competition scrutiny regime in the Companies Act and consequential exclusion from the Competition Act.

Provisions concerning Environmental Protection Producer Responsibility Schemes

5.16 The Environment Act makes provision for imposing obligations on certain persons for the purposes of increasing recycling of certain products or materials when they are waste, for example, packaging and

⁵⁹ The notifications procedure is contained within sections 12 to 16 and 21 to 24 of the Competition Act.

⁶⁰ For further information see section 3 of our earlier consultation: for details see footnote 1.

packaging waste. These are known as “Producer Responsibility Obligations”. The powers in the Environment Act have been used to make regulations (‘the 1997 Regulations’)⁶¹ which govern the recovery and recycling of packaging waste. “Producers” under these Regulations can form a “compliance” scheme, which must be registered by the appropriate Agency, for example, the Environment Agency in England and Wales. Registered schemes discharge the producer responsibility obligations on behalf of their members and thereby serve to exempt their members from the legal requirement to comply with the producer responsibility obligations.

5.17 Section 94 of the Environment Act, when it came into force, provided for:

- competition scrutiny of registered exemption schemes or of exemption schemes for which applications for registration had been made⁶²; and
- exclusion or modification of any provision of the RTPA in relation to exemption schemes or in relation to agreements where at least one of the parties was an operator of an exemption scheme⁶³.

5.18 The 1997 Regulations established a competition scrutiny regime for exemption schemes and the Competition Act amended the Environment Act by repealing the exclusion from the RTPA and replacing it with a power to exclude or modify any provision of Part I of the Competition Act in relation to exemption schemes or agreements, decisions or concerted

⁶¹ See footnote 46.

⁶² Environment Act section 94(1)(n)

⁶³ Environment Act section 94(1)(o). Section 94(6) defined exemption scheme as “a scheme which is (or, if it were to be registered in accordance with the regulations, would be) a scheme whose members for the time being are, by virtue of the regulations and their membership of that scheme, exempt from the requirement to comply with the producer responsibility obligation imposed by the regulations.”

practices in which at least one of the parties was an operator of an exemption scheme.

5.19 After these amendments, the 1997 Regulations were themselves amended in 1999 to repeal the separate competition scrutiny regime⁶⁴. Producer Responsibility Schemes now fall to be considered under the Competition Act.

5.20 There is still provision in the Environment Act for:

- the creation, by Regulation, of a new competition scrutiny regime for producer responsibility schemes;
- the exclusion of such schemes from the Chapter I and Chapter II prohibitions of the Competition Act.

5.21 As discussed elsewhere in this section (paragraphs 5.3 to 5.5), the Regulation may place some constraints on the effective operation of competition scrutiny regimes where the agreements or practices they concern have an effect on trade between Member States. The Government's aim in giving effect to the Regulation is to align the domestic regime with the EC system so that, as far as practicable, the competition authorities are operating consistently irrespective of whether they are applying the Chapter I and II prohibitions or Articles 81 and 82. In this context, the Government believes it is generally not desirable to create new competition scrutiny regimes, as these increase the potential for inconsistent approaches to arise. The Government also believes that, in principle, sectors of the economy should not be singled out for special treatment unless there are compelling policy reasons to do so and the Competition Act should therefore apply.

⁶⁴ See footnote 46.

The Government proposes to repeal the provisions of the Environment Act that allow for the creation of a separate competition scrutiny regime for Producer Responsibility Schemes and for the exclusion of such schemes from the Competition Act. We welcome your views on this proposal.

6. AGREEMENTS GIVEN DIRECTIONS UNDER SECTION 21(2) OF THE RESTRICTIVE TRADE PRACTICES ACT 1976

6.1 This exclusion concerns agreements benefiting from directions by the Secretary of State under section 21(2) of the Restrictive Trade Practices Act 1976 (RTPA). When the Competition Act was introduced, a separate exclusion was created for agreements benefiting from directions by the Secretary of State under section 21(2) of the RTPA, such that the restrictions or information provisions they contained were considered not to be of such significance to call for investigation by the Restrictive Practices Court. The majority of agreements made before the enactment date of the Competition Act, which were furnished to the Director General of Fair Trading under the RTPA, had the benefit of section 21(2) directions and were considered generally not to be of concern under the new regime⁶⁵.

6.2 Paragraph 2 of Schedule 3 to the Competition Act excludes from the Chapter 1 prohibition those agreements where a direction given under section 21(2) of the RTPA was in force immediately before the coming into force of section 2 of the Competition Act. The protection granted by the exclusion is removed if the agreement that is subject to the section 21(2) direction is varied, or if the OFT issues a direction to withdraw the benefit of the exclusion (a "claw back")⁶⁶.

6.3 It is not known how many agreements currently in operation benefit from a section 21(2) direction. While these directions were generally granted for a specific period (normally 7 years), the effect of Schedule 3 paragraph 2 is to grant a permanent exclusion from the

⁶⁵ Transitional Arrangements, OFT 406, March 1999

⁶⁶ Under paragraph 6(b) of Schedule 13 to the Competition Act, it ceased to be possible for agreements to obtain a section 21(2) direction on 9th November 1998. See also Transitional Arrangements, OFT 406, March 1999, para 4.14.

Chapter I prohibition, subject to variation of the agreement and the possibility of clawback.

6.4 To remove the exclusion now might have little adverse effect on business. Arguably, the protection and legal certainty afforded by this exclusion is limited. Firstly and most importantly, it provides no protection from Article 81 for those agreements that may affect trade between Member States. Secondly, there is a clawback. Thirdly, the exclusion can cease to have effect if the agreement is varied. Finally, even if the exclusion ceases to have effect, it does not follow that the agreement in question would automatically infringe Chapter I of the Competition Act, as it may not prevent, restrict or distort competition within the meaning of section 2 of the Competition Act, or it may meet the criteria of section 9 of the Competition Act⁶⁷. Many of these agreements may fall outside of the Chapter I (and Article 81) prohibitions altogether because they are likely to have no appreciable effect on competition.

The Government seeks your views on whether to remove the exclusion from the Competition Act for agreements given clearance under section 21(2) of the Restrictive Trade Practices Act 1976, and on the number of agreements that might be affected if the exclusion were to be removed.

⁶⁷ See footnote 27.

ANNEX A - COMPARISON OF TREATMENT OF VERTICAL AGREEMENTS UNDER UK AND EC LAW

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Relevant market share, % ⁶⁸	Treatment of vertical agreements which have no actual or potential effect on trade between member states and so subject to CA98 only		Treatment of vertical agreements which may affect trade between member states and so subject to A81 and A82	Effect of change on UK regime
	Existing CA98 regime	Proposed New CA98 regime	EC Regime	Comparing existing and proposed new CA98 regimes
40+	Ch II applies if undertaking is dominant ⁶⁹ and is abusing that dominant position. Excluded from Ch I under the Order if relevant criteria are satisfied, unless contains RPM clause, but subject to "claw back" ⁷⁰	Ch II applies if undertaking is dominant ⁷¹ and is abusing that dominant position. Subject to Ch I if appreciable anti-competitive effects on competition	A82 applies if undertaking dominant and is abusing that dominant position. Subject to A81 if appreciable anti-competitive effects on competition	Ch II - no change Ch I - no substantial change: agreements which have appreciable anti-competitive effects on competition subject to scrutiny under both regimes
30-40	Excluded from Ch I under the Order if relevant criteria are satisfied, unless contains RPM clause, but subject to "claw back" ⁷²	Subject to Ch I if appreciable anti-competitive effects on competition.	Subject to A81 if appreciable anti-competitive effects on competition.	No substantial change - agreements which have appreciable anti-competitive effects on competition subject to scrutiny under both regimes

⁶⁸ This will usually be the market share of the supplier save in the case of exclusive supply obligations where the relevant market share will be that of the buyer

⁶⁹ Dominance can be presumed in the absence of evidence to the contrary if an undertaking has a market share persistently above 50%. It is unlikely that an undertaking will be individually dominant if its market share is below 40% although it could be established if there are other relevant factors.

⁷⁰ The OFT can withdraw the Order in certain circumstances e.g. where the agreement, if not excluded, will infringe Ch I and is unlikely to benefit from an unconditional individual exemption.

⁷¹ See footnote 69.

⁷² See footnote 70.

0-30	Excluded from Ch I by virtue of the Order if the relevant criteria are satisfied, unless contains RPM clause, but subject to “claw back” ⁷³ . If an agreement falls outside the Order it will infringe Ch I only if it has an appreciable anti-competitive effect on competition, which is unlikely if the combined market share of the undertakings is below 25% ⁷⁴	If appreciable anti-competitive effects on competition, an agreement may benefit from the BER by virtue of a parallel exemption ⁷⁵ if all the relevant criteria are satisfied ⁷⁶ unless it includes a BER ‘hard core’ restriction. An agreement is unlikely to have any appreciable anti-competitive effects if the combined market share of the undertakings is below 25% ⁷⁷	If appreciable anti-competitive effects on competition, an agreement may benefit from the BER if all the relevant criteria are satisfied ⁷⁸ unless it includes a BER ‘hard core’ restriction. Unlikely to have any appreciable anti-competitive effects if it falls under the Commission’s Notice on agreements of minor importance ⁷⁹ .	No substantial change - agreements which have an appreciable anti-competitive effect on competition are subject to scrutiny under both regimes. While vertical agreements which include BER ‘hard core’ restrictions other than RPM clauses are arguably subject to greater scrutiny under the proposed new regime, these agreements would be of concern to the OFT only if they have appreciable anti-competitive effects. An agreement is unlikely to have any appreciable anti-competitive effects if the combined market share of the undertakings is below 25% ⁸⁰
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This table is for illustrative purposes only. It focuses on general principles relevant to a high level comparison of the Exclusion Order and the BER. It is therefore not an exhaustive or definitive guide to the treatment of vertical agreements under either the UK or the EU competition regimes.

⁷³ See footnote 70.

⁷⁴ Combined market share refers to shares in the same relevant market; note that the OFT will generally regard vertical agreements which directly or indirectly impose minimum resale prices or which are one of a network of agreements that have a cumulative effect on the relevant market as being appreciable even if the combined market share of the parties is below 25%

⁷⁵ Section 10(1)(a) CA98 NB: The OFT can *inter alia* impose conditions or obligations subject to which a parallel exemption may take effect (section 10(5) CA98)

⁷⁶ NB: the exemption can be cancelled (section 10(5) CA98)

⁷⁷ See footnote 74.

⁷⁸ NB: the BER can be withdrawn (Art 6 BER) or disapplied (Art 8 BER) in certain circumstances

⁷⁹ OJ 2001/C 368/07

⁸⁰ See footnote 74.

ANNEX B – FOUR CATEGORIES OF EXCLUSIONS FROM THE CHAPTER I AND/OR CHAPTER II PROHIBITIONS UNDER THE COMPETITION ACT 1998 (THE CA98) (THE CA98 PROHIBITIONS)⁸¹

Category 1 – Exclusions from the CA98 prohibitions for agreements or conduct that are likely to have little or no effect on trade between Member States

Exclusion	Source	Scope	Categorisation
<p>Land agreements (i.e. agreements between undertakings which create, alter, transfer or terminate an interest in land, or agreements to enter into such agreements) as well as obligations and restrictions which relate to relevant land. To the extent that the agreement is a vertical agreement it is not a land agreement.</p>	<p>The Competition Act (Land and Vertical Agreements Exclusion) Order 2000 (SI 2000/310), made under section 50 CA98</p>	<p>The Chapter I prohibition shall not apply to an agreement to the extent that it is a land agreement.</p> <p>The exclusion is designed to remove from the Chapter I prohibition many of the restrictive covenants typically entered into in land agreements: see Article 6 of the Order, and section 2 of OFT Guideline 420.</p> <p>There is no exclusion from the Chapter II prohibition.</p>	<p>An effect on inter-state trade can never be entirely ruled out, but the risks would appear to be relatively low.</p>

⁸¹ This annex is for illustrative purposes only and does not purport to be a definitive guide or exhaustive description of the scope of exclusions from the CA98 Prohibitions.

<p>Planning obligations</p>	<p>Schedule 3 paragraph 1 CA98</p>	<p>Agreements which are</p> <ul style="list-style-type: none"> • planning obligations for the purposes of sections 106 or 299A of the Town and Country Planning Act 1990; • made under sections 75 or 246 of the Town and Country Planning (Scotland) Act 1997; or • made under Article 40 of the Planning (Northern Ireland) Order <p>are excluded from the Chapter I prohibition.</p> <p>There is no exclusion from the Chapter II prohibition.</p>	<p>Effect on inter-state trade can never be entirely ruled out, but the risks would appear to be low.</p>
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Category 2 – exclusions from the CA98 prohibitions for agreements or conduct where there could be an effect on trade between Member States but for which there is equivalent treatment under EC law in respect of the application of Articles 81 and/or 82

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Exclusion	Source	Scope	Categorisation
<p>Merger situations under Part V of the Fair Trading Act 1973 (FTA) and/or Part 3 of the Enterprise Act 2002 (EA).</p>	<p>Schedule 1 paragraphs 1-5 CA98</p>	<p>To the extent to which one or more agreements would result in any two enterprises ceasing to be distinct for the purposes of Part V FTA/Part 3 EA, the Chapter I prohibition does not apply to it/them. This exclusion extends to any provision directly related and necessary to the implementation of those provisions of the agreements which would result in two enterprises ceasing to be distinct.</p> <p>To the extent to which conduct results in any two enterprises ceasing to be distinct for the purposes of Part V FTA/Part 3 EA, the Chapter II prohibition does not apply to that conduct. This exclusion extends to any provision directly related and</p>	<p>Article 3(3) of Regulation 1/2003 states that the requirement in Article 3(1) and 3(2) to apply Article 81 and 82 in parallel to national law in any case which may affect trade between member States will not apply when the NCA is applying national merger control laws.</p>

		<p>necessary to the attainment of the two enterprises ceasing to be distinct.</p> <p>Similar exclusions apply to agreements and conduct resulting in the transfer of newspaper assets.</p>	
<p>Concentrations with a Community dimension under the EC Merger Regulation (Council Regulation 4064/89, as amended) (the ECMR)</p>	Schedule 1 paragraph 6 CA98	<p>Agreements or conduct giving rise to a concentration over which the European Commission has exclusive jurisdiction under the ECMR are excluded from the CA98 prohibitions.</p>	<p>Article 21(2) of the ECMR provides that the ECMR alone shall apply to all concentrations with a Community dimension.</p>
<p>Services of general economic interest</p>	Schedule 3, paragraph 4 CA98	<p>Neither the Chapter I nor the Chapter II prohibition applies to an undertaking entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly in so far as the prohibition would obstruct the performance, in law or fact, of the particular tasks assigned to that undertaking.</p>	<p>The exclusion is based on Article 86(2) of the EC Treaty.</p>
<p>Compliance with legal requirements (requirements imposed by or under any enactment in force in the UK, imposed by or under the EC Treaty or the EEA Agreements and having legal effect in the UK without further enactment, or imposed by or under the law in force in another Member State and having legal effect in the UK).</p>	Schedule 3, paragraph 5 CA98	<p>The Chapter I prohibition does not apply to an agreement to the extent to which it is made in order to comply with a legal requirement, and the Chapter II prohibition does not apply to conduct to the extent that it is engaged in order to comply with such a requirement.</p>	<p>An equivalent exclusion applies following from case law of the ECJ (see Joined cases C-359/95 P and C-379/95 P, <i>Commission and France v. Ladbroke Racing Ltd</i>, judgment of 11 November 1997).</p>

Agricultural products	Schedule 3, paragraph 9 CA98	<p>The Chapter I prohibition does not apply to agreements to the extent to which they relate production of or trade in an agricultural product listed in Annex II to the EC Treaty and which</p> <ul style="list-style-type: none"> • form an integral part of a national market organisation; • are necessary for attainment of the objectives set out in Article 39 of the EC Treaty; or • are agreements of farmers (or their associations) belonging to a single Member State which concern the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of agricultural products, <p>and under which there is no obligation to charge identical prices.</p> <p>There is no exclusion from the Chapter II prohibition.</p>	An equivalent exclusion applies under EC law in respect of Article 81 in terms of Regulation 26/62/EC.
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Category 3 – exclusions from the CA98 prohibitions for agreements or conduct where there could be an effect on trade between Member States and for which the treatment under EC law in respect of the application of Articles 81 and/or 82 differs in scope from our domestic exclusion

Exclusion	Source	Scope	Categorisation
Vertical agreements (agreements between undertakings, each of which operates, for the purposes of the agreements, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services, including provisions contained in such agreements which relate to the	The Competition Act 1998 (Land and Vertical Agreements Exclusion) Order 2000 (SI 2000/310) (the Order) made under section 50 CA98	<p>Under Article 3 of the Order, the Chapter I prohibition shall not apply to an agreement to the extent that it is a vertical agreement.</p> <p>However, the exclusion does not apply where the vertical agreement, directly or indirectly, in isolation or in combination with other factors under the control of the parties has the</p>	Many vertical agreements may have an effect on trade between member states, in which case the parties will also need to consider the application of Article 81 and the possibility of benefiting from an exemption under the EC block exemption regulation 2790/99/EC (the BER). The BER is structured differently from the UK exclusion. If the BER applies to an

<p>assignment to the buyer or use by the buyer of intellectual property rights, provided that those provisions do not constitute the primary object of the agreement and are directly related to the use, sale or resale of goods or services by the buyer or its customers).</p>		<p>object or effect of restricting the buyer's ability to determine its sale price, without prejudice to the possibility of the supplier imposing a maximum sale price or recommending a sale price, provided that these do not amount to a fixed or minimum sale price as a result of pressure form, or incentives offered by, any of the parties.</p> <p>There is no exclusion from the Chapter II prohibition.</p>	<p>agreement, that agreement will automatically benefit from a parallel exemption from the Chapter I prohibition by virtue of section 10 CA98, subject to the power of the OFT to cancel the exemption or attach conditions or obligations.</p>
<p>Avoidance of conflict with international obligations</p>	<p>Schedule 3, paragraph 6 CA98</p>	<p>To avoid conflict between the provisions of CA98 and an international obligation of the UK (including an international arrangement relating to civil aviation), the Secretary of State may by order provide that the Chapter I prohibition does not apply to an agreement, or agreements of a particular description, or that the Chapter II does not apply to specified conduct.</p>	<p>This exclusion relates at least in part to the UK's obligations under Article 10 of the EC Treaty (i.e. to ensure fulfilment of the obligations arising out of the EC Treaty), but is potentially broader.</p> <p>However, it would be necessary to apply this exclusion strictly in line with European law so as to comply in any case with Article 10 of the EC Treaty, therefore in reality, this exclusion, if exercised, would be unlikely to conflict with EC Competition Law.</p>

Category 4 – exclusions from the CA98 prohibitions for agreements or conduct where there could be an effect on trade between Member States and for which there is no equivalent treatment under EC law in respect of the application of Articles 81 and/or 82

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Exclusion	Source	Scope	Categorisation
<p>Statutory Audit Services</p> <p>Rules made and guidance issued by accountancy bodies, which are applying for, or have been granted, the status of “recognised supervisory body” (RSB) or “recognised qualifying body” (ROB).</p> <p>Any practices of RSBs or ROBs in their capacity as such; any relevant practices required or contemplated by the rules or guidance of RSBs or ROBs to their conduct in their capacity as such.</p> <p>For these purposes, “practices” are (in the case of RSBs) practices engaged in for the purposes of, or in connection with, appointment as a company auditor, or for the conduct of company audit work by persons eligible under their rules for appointment as a company auditor; and (in the case of ROBs) practices engaged in by persons seeking to obtain a recognised professional qualification from them and by persons approved by them for the purposes of giving practical training to those seeking such a qualification.</p>	<p>Schedule 2, Part II CA98, Schedule 14 to Companies Act 1989 and The Companies (Northern Ireland) Order 1990 (SI 1990/593 (NI 5))</p>	<p>The Chapter I prohibition does not apply to:</p> <ul style="list-style-type: none"> • rules made by and guidance issued by an ROB or RSB; • incidental matters connected with such rules and guidance; • an agreement to which a recognised body or a person subject to a ROB or RSB or a person eligible under its rules to be appointed as a company auditor or persons approved to provide practical training for an auditing qualification is party, to the extent which the agreement consists of provisions the inclusion of which is required or contemplated by the rules or guidance of the body concerned. <p>There is no exclusion from the Chapter II prohibition.</p>	<p>No equivalent EC exclusion/exemption. Case law of the European Court indicates that where regulation covers the whole of a profession in the territory of a Member State, inter-state trade is likely to be affected. See, for example, the <i>Wouters</i> case, which has the effect that many of the rules which may benefit from the exclusion may be subject to Article 81.</p>
<p>Channel 3 news provision</p>	<p>Schedule 2, Part III CA98</p> <p>Section 194A Broadcasting Act 1990</p> <p>Part 4 Communications Bill</p>	<p>Agreements for securing the appointment by holders of Channel 3 licences of a single body corporate to be the appointed news provider for the purposes of section 31(2) of the</p>	<p>No equivalent EC exclusion/exemption.</p>

		<p>Broadcasting Act 1990 may be exempted from the Chapter I prohibition to the extent to which the Secretary of State has made a declaration to this effect.</p> <p>There is no exclusion from the Chapter II prohibition.</p>	
Channel 3 networking arrangements	<p>Schedule 2, Part III CA 1998</p> <p>Section 39 and Schedule 4 Broadcasting Act 1990</p> <p>Part 4 Communications Bill</p>	<p>The Chapter I prohibition does not apply to the Channel 3 networking agreements to the extent to which they are subject to the special competition regime in Schedule 4 of the Broadcasting Act 1990 (list of such agreements to be published by ITC).</p> <p>There is no exclusion from the Chapter II prohibition.</p>	No equivalent EC exclusion/exemption.
Environmental protection	<p>Schedule 2, Part IV CA 1998</p> <p>Section 94 Environment Act 1995</p>	<p>Regulations imposing producer responsibility obligations on prescribed persons may provide for the exclusion or modification of the Chapter I prohibition in so far as it would apply to exemption schemes.</p> <p>There is no equivalent provision for exclusion from the Chapter II prohibition.</p>	No equivalent EC exclusion/exemption.
Agreements given section 21(2) clearance under the Restrictive Trade Practices Act 1976 (the RTPA)	Schedule 3, paragraph 2 CA 1998	<p>The Chapter I prohibition does not apply to agreements which are the subject of a direction under section 21(2) of the RTPA.</p> <p>If a material variation is made, the exclusion shall cease to apply from the date of the variation (paragraph 2(2) of Schedule 3).</p> <p>There is no exclusion from the Chapter II prohibition.</p>	No equivalent EC exclusion/exemption.

<p>Public policy</p>	<p>Schedule 3, paragraph 7 Competition Act 1998</p>	<p>The Secretary of State may by order exclude any agreement or conduct from the application of the Chapter I or Chapter II prohibitions where he is satisfied that there are exceptional and compelling reasons of public policy to do so. For example, the power could be invoked in relation to the defence industry.</p>	<p>No directly equivalent EC exclusion/exemption although Article 296 of the EC Treaty excludes from the EC competition rules certain matters relating to defence, which may catch certain orders made pursuant to this exclusion.</p> <p>However, in any event, it would be necessary to apply this exclusion strictly in line with European law (to comply with the UK's obligations under Article 10 of the EC Treaty), therefore in reality the application of this exclusion would fall within category 1 or 2.</p>
<p>Financial services regulation (general)</p> <p>"Regulating provisions" (i.e. rules made, general guidance, statements and codes issued by the Financial Services Authority (FSA) under various provisions of FSMA and "practices" adopted by FSA in exercise of its functions under FSMA).</p> <p>The OFT is under a duty to keep regulating provisions and practices under review, using the special competition test.</p> <p>Note that there is also an order-making power to apply similar regimes in other areas (section 95 FSMA).</p>	<p>Sections 169-164 FSMA</p>	<p>The Chapter I prohibition does not apply to agreements to which authorised persons, or others subject to FSA regulating provisions, are party, to the extent that it consists of provisions the inclusion of which is encouraged by FSA's regulating provisions.</p> <p>The Chapter II prohibition does not apply to conduct of these classes of persons to the extent that it is encouraged by FSA regulating provisions.</p>	<p>No equivalent EC exclusion/exemption, but note stipulations of Investment Services Directive (Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field).</p>
<p>Financial services regulation (investment exchanges) Practices of recognised investment exchanges in their capacity as such and of clearing houses in respect of their clearing arrangements.</p> <p>"Regulatory provisions" (i.e. rules of recognised investment exchanges or clearing houses; guidance issued by</p>	<p>Sections 302-312 Financial Services and Markets Act 2000</p>	<p>The Chapter I prohibition does not apply to:</p> <ul style="list-style-type: none"> • an agreement for the constitution of a recognised body to the extent to which the agreement relates to the regulatory provisions of that body; • an agreement for the constitution of an investment exchange which 	<p>No equivalent EC exclusion/exemption but note stipulations of Investment Services Directive (Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field).</p>

<p>them; and the arrangements and criteria for providing clearing services which they have furnished to the FSA with their application for recognition). Regulatory provisions are scrutinised before an application for recognition is granted by the FSA; the OFT is also under a duty to keep regulatory provisions and practices under review using the special competition test.</p>		<p>is not a recognised investment exchange, or a clearing house which is not a recognised clearing house, if the body has applied for a recognition order which has not been determined.</p> <ul style="list-style-type: none"> • a recognised body's regulatory provisions or practices; • a decision made by a recognised body to the extent to which it relates to that body's regulatory provisions or practices; • an agreement to which a recognised body or a person subject to a recognised bodies rules is a party, to the extent that it consists of provisions the inclusion of which is required or encouraged by any of the body's regulatory provisions or practices. <p>The Chapter II prohibition does not apply to recognised body's practices or (adoption or enforcement of) regulatory provisions; or to conduct engaged in by a recognised body or a person subject to the rules of a recognised body to the extent that it is encouraged or required by the regulatory provisions of that body.</p>	
<p>Securities trading in EEA regulated markets (i.e. markets which are listed by an EEA State other than the UK pursuant to Article 16 or Council Directive No 93/22 of 10th May 1993 on investment services in securities and which operate without any requirement that a person dealing on the market should have a physical presence in the EEA State from which any trading facilities are provided or on any trading floor that the market may have)</p>	<p>Schedule 3, paragraph 3 Competition Act</p>	<p>The Chapter I prohibition does not apply to:</p> <ul style="list-style-type: none"> • agreements constituting an EEA regulated market to the extent to which it relates to any of the rules made, or guidance issued, by that market; • decisions made by an EEA regulated market to the extent to which it relates to its regulating provisions; • practices of, or trading practices in relation to an EEA regulated 	<p>No equivalent EC exclusion/exemption.</p>

		<p>relation to an EEA regulated market;</p> <ul style="list-style-type: none">• agreements relating to regulating provisions of an EEA regulated market to which an EEA regulated market or a person subject to the rules of such a market are parties. <p>This exclusion was designed to give EEA regulated markets the same treatment under CA98 as was given to recognised investment exchanges under section 125 of the Financial Services Act as amended by CA98 (equivalent to the current FSMA regime).</p> <p>There is no exclusion from the Chapter II prohibition.</p>	
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ANNEX C – LIST OF CONSULTEES

3i Group
Accountancy Foundation
Addleshaw Booth & Co.
Advertising Association
Advertising Standards Authority
AIM UK
Airbus
Allen & Overy
Alliance of Independent Retailers & Business
Amicus (Aerospace)
Apparel, Footwear & Textile Sector Skills Council
Ashurst Morris Crisp
Association of British Health-Care Industries
Association of Certified Chartered Accountants
Association of Franchised Distributors of Electronic Components
Association of Learned and Professional Society Publishers
Association of Lloyds Members
Association of Manufacturers of Domestic Appliances
Association of Newspaper & Magazine Wholesalers
Association of Police and Public Security Suppliers
Association of Train Operating Companies
AstraZeneca
BA
BAE Systems
BAFTA
Baker & McKenzie
Barclays plc
BBC
BHP Billiton Plc
BP
British Airways
British Apparel and Textiles Confederation/British Clothing Industry Association
British Brands Group
British Ceramic Confederation
British Chamber of Commerce in Brussels
British Chambers of Commerce
British Computer Society

British Fashion Council
British Footware Association (incl NFMA)
British Franchise Association
British Institute of International & Comparative Law
British Jewellers Association
British Leather Confederation
British Marine Foundation
British Metals Recycling Association
British Printing Industries Fed
British Retail Consortium
British Security Industries Association
British Shop & Stores Association
British Sky Broadcasting Ltd
Bruce Lyons
BT
Business Services Association
Business Tourism Partnership
Cable & Wireless
Call Centre Association
Cardiff Chamber of Commerce
Carpet Foundation
Cast Metals Federation
Centrica plc
CGNU
Chris Kerse (European Communities Committee)
CIPFA
Civil Aviation Authority
Clifford Chance
CMS Cameron McKenna
Colin Challen MP
Colt Telecommunications on behalf of the Operators
Companies Registry Belfast
Compass Group
CompEcon Limited
Competition Commission
Competition Law Association
Confederation of British Industry
Confederation of British Metalforming
Confederation of Paper Industries

Confederation of Passenger Transport
Construction Confederation
Construction Industry Council
Construction Industry Training Group
Construction Products Association
Consumers' Association
Consumers in European Community Group
Corus
Council on Tribunals
Defence Manufacturers Association
Deloitte & Touche
Diageo
Digital Content Forum
Direct Marketing Association
Directories & Database Publishers Association
Ernst & Young
European Commission
European Health Telematics Association
European Leisure Software Publishers Association
Federation of Small Businesses
Financial Services Authority
Fire Industry Confederation
First Choice
Forum of Private Business
Foundation for the Built Environment
FRC
Freshfields Bruckhaus Deringer
GAMBICA
GEC Marconi
Giftware Association
GKN
GlaxoSmithKline
Green Party
Herbert Smith
ICAS
Independent Television Commission
Industry Forum
Innogy
Institute of Chartered Accountants in England and Wales

Institute of Chartered Accountants in Ireland
Institute of Chartered Accountants in Scotland
Institute of Directors
Institute of Public Relations
Intellect
Interconnection Technology Industrial Consortium
International Association of Broadcasting Manufacturers
International Chamber of Commerce
Internet Service Provider Association
Jeremy Lever QC
Joint Equipment and Materials Initiative
Joint Industry Group (Newspaper & Magazine Supply Chain)
Joint Security Industry Council
Kingfisher
KPMG
Latham & Watkins
Lattice group
Law Society for Northern Ireland
Law Society of Scotland
Laytons
Linklaters
London Electricity
Lovells
Manufacturing Technologies Association
Mark Furse
Martin Howe
Merseytravel
Metal Packaging Manufacturing Association
METCOM
Michael Hutchings
Microsystems Manufacturing Association
Mid-Yorkshire Chamber of Commerce and Industry
Morgan Cole Solicitors
My Travel Plc
Nabarro Nathanson
National Association of Citizens Advice Bureaux
National Audit Office
National Consumer Council
National Federation of Retail Newsagents

National Microelectronics Institute
Newspaper Publishers Association
Newspaper Society
Nonwovens Network
Northumbrian Water
Norton Rose
Olswang
P & O Princess Cruises Ltd
Periodical Publishers Association
Permira
Postcomm
Pricewaterhouse Coopers
Printed Circuit Interconnection Federation
Public Concern at Work
Radio, Electrical & Television Retailers Association Ltd
Rail Industry Association
Rail Passengers Council
Railway Forum
RBB Economics
Rethinking Construction Ltd
Rexam
Richard Whish
Richards Butler
S J Berwin
Scottish & Newcastle
Scottish Consumer Council
Semiconductor Business Association
Shearman & Stirling
Shell
Ship Mortgage Finance Corporation plc
Shipbuilders and Shiprepairers Association
Simkins Partnership
Simmons & Simmons
Slaughter & May
SMART Group
SMMT Industry Forum
Society of British Aerospace Companies
Society of Maritime Industries
Society of Motor Manufacturers and Traders Ltd

Specialised Organic Chemicals Sector Association
Stephenson Harwood
Stoy Hayward
Strategic Rail Authority
Surface Engineering Association
TAHI (The Application Homes Initiative)
Taylor Joynson Garrett
Telecommunications Industry Association
Tesco Plc
Textile and Clothing Strategy Group
The Chamber of Shipping
The City of London Law Society
The Gin and Vodka Association
The Law Society
The Newspaper Society
The Publishers Association
The Scotch Whisky Association
TIGA (Independent game developers association)
T-mobile
Tom Sharpe QC
Trading Standards Institute
Transco
Travers Smith Braithwaite
TUC
UK eHealth Assoc.
UK Steel
UNIFI
Unilever
Valentine Korah
Vodafone Plc
Wales IOD
Water UK
WaterVoice
Welsh CBI
Welsh Consumers Council
Wragge & Co
Zoltan Biro

ANNEX D – PARTIAL REGULATORY IMPACT ASSESSMENT

GIVING EFFECT TO COUNCIL REGULATION 1/2003 – CONSIDERATION OF EXCLUSIONS

1. PURPOSE AND INTENDED EFFECT OF MEASURE

Objective

1.1 This proposal seeks to create alignment between the treatment of agreements and conduct under the Competition Act 1998 ('the Competition Act') and their treatment under the EC Treaty Articles on competition (Articles 81 and 82). The focus of this proposal is on those agreements or conduct which carry a significant risk of falling to be considered under EC law because they have an effect on trade between Member States.

Background

1.2 Articles 81 and 82 are currently implemented by Council Regulation 17/62. Regulation 1/2003 ('the Regulation'), which come into force on 1st May 2004, replaces this Regulation and modernises the implementation of Articles 81 and 82 by:

- replacing the current system under which agreements can be notified with a legal exception regime;
- devolving much of the enforcement of Community competition law to the National Competition Authorities (NCAs) and courts of Member States; and

- requiring these authorities to apply Community law to all cases capable of affecting trade between Member States (although this may be in parallel to proceedings under national law if the Member State wishes).

1.3 The Government's proposals for giving effect to Regulation 1/2003 are discussed in our earlier consultation document "Modernisation – a consultation on the Government's proposals for giving effect to Regulation 1/2003EC and for re-alignment of the Competition Act 1998"⁸² which includes a separate Regulatory Impact Assessment.

1.4 Articles 81 and 82 apply to agreements and conduct that affect trade between Member States whereas the Competition Act applies to agreements and conduct that have an effect on trade within the UK. Certain types of agreement or conduct may be treated differently under the Competition Act either because they have been excluded from the scope of the Act altogether or because, in the case of agreements, they are subject to an individual or block exemption. Exemptions may be granted where an agreement is restrictive of competition but where the effects of the restriction are outweighed by the benefits of the agreement⁸³.

1.5 It is possible at present for an agreement to be excluded from our domestic competition law yet be caught by Article 81. The Regulation does

⁸² UK Competition Law: Modernisation – a consultation on the Government's proposals for giving effect to Regulation 1/2003 EC and for re-alignment of the Competition Act 1998, April 2003, URN 03/750 available at <http://www.dti.gov.uk/ccp/consultpdf/compmocon.pdf> and in hard copy by ordering from DTI Publications online at: <http://www.dti.gov.uk/publications/>

⁸³ An exemption may be applicable to "any agreement which contributes to improving production or distribution, or promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit; but does not impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; or afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question". Section 9, Competition Act

not alter this position. However, it does require the Office of Fair Trading ('the OFT') and the sectoral regulators⁸⁴ to apply Articles 81 and 82 in full for the first time and to require that these NCAs apply Article 81, in parallel to national competition law, in any case where there is an effect on inter-state trade. From 1st May 2004 therefore, the same competition authorities which are barred from applying the Chapter I prohibition, by virtue of an exclusion or an exemption, will be required to apply Article 81 to the same agreement if it affects trade between Member States. The Government believes that the treatment of agreements and conduct should be similar under both EC and UK law wherever possible and that the Competition Act should be re-aligned with the new European system as it will look once the Regulation comes into force. The consequence of not ensuring that the two systems are aligned would be greater legal uncertainty and a higher regulatory burden on business. The Government is therefore proposing to minimise the differences between EC competition law and the Competition Act as far as is practicable.

Risk Assessment

1.6 The main risk addressed by the Regulation is that the lack of a common approach to enforcing EC competition rules could fragment the Single Market leading to ineffective competition. This would reduce innovation, efficiency and productivity within the Single Market, which would translate into higher prices for consumers. The Regulation aims both to strengthen enforcement and to reduce certain barriers to cross-border competition in the EU thereby promoting effective competition.

⁸⁴ OFTEL (shortly to be incorporated into OFCOM), OFGEM, OFWAT, OFREG NI, ORR and CAA all have concurrent powers under the Competition Act

1.7 The Statutory Instrument implementing the Regulation and aligning the UK competition regime will address the risks that differential application of two separate legal bases by the same UK NCAs could increase compliance burdens on business and reduce the efficiency and effectiveness of competition law enforcement.

2. OPTIONS CONSIDERED

2.1 There are two main options to consider for each exclusion from the Competition Act: keeping the exclusion, or repealing it. Where relevant, a further option of amending the exclusion is considered. . This RIA deals with those exclusions that we intend to either amend or repeal to create alignment with the European system. It does not deal with exclusions from the Competition Act that relate to agreements or conduct where there is only a small risk that such agreements or conduct might fall to be considered under the EC Treaty Articles on competition. Nor does it deal with exclusions from the Competition Act that closely follow equivalent exclusions at EC level. The Government sees no reason to remove exclusions where either of these two conditions pertains⁸⁵.

2.2 The exclusions that the Government proposes to amend or repeal are:

- (i) the domestic Exclusion Order for Vertical Agreements⁸⁶

⁸⁵ We have also not addressed certain exclusions in Schedule 2 and Schedule 3 to the Competition Act in relation to broadcasting and financial services. The exclusions concerning broadcasting and their corresponding competition scrutiny regime will become the responsibility of OFCOM when it is established and those concerning financial services are to be considered as part of a wider review of the Financial Services and Markets Act 2000, announced by the Chancellor of the Exchequer in August 2000.

⁸⁶ The Competition Act 1998 (Land and Vertical Agreements Exclusion) Order 2000, SI 2000/310

- (ii) the exclusion for the rules, guidance and practices of recognised supervisory or qualifying bodies for Statutory Audit and the related competition scrutiny regime under the Companies Act 1989('the Companies Act')⁸⁷
- (iii) the exclusion for agreements given clearance under section 21(2) of the Restrictive Trade Practices Act 1976 ('the RTPA')⁸⁸
- (iv) the power to exclude from the Competition Act 1998 Producer Responsibility Schemes under the Environment Act 1990⁸⁹.

2.3 The Government also proposes to remove provisions in the Competition Act that enable the inclusion of "opposition procedures" (a kind of "fast-track" notification for agreements which fall marginally outside the scope of a block exemption) in a Block Exemption Order. These provisions have never been used and their removal will have no impact on business. They are therefore not discussed further here. As there are no regulations currently governing Producer Responsibility Schemes, the removal of the power in the Environment Act will also have no effect and is also not discussed further here.

Vertical Agreements

2.4 Vertical agreements are agreements made between bodies operating at different levels in the supply chain, for example between manufacturers and wholesalers or retailers. Typical vertical agreements include distribution agreements, purchasing agreements, selective distribution agreements and franchise agreements. There are two options under consideration for vertical agreements under the Competition Act: keeping the domestic Exclusion

⁸⁷ Schedule 14, paragraph 9 to the Companies Act 1989 as amended by the Competition Act 1998, Schedule 2, Part II, paragraphs 2(1) and 2(2)

⁸⁸ Schedule 3, paragraph 2 to the Competition Act 1998

⁸⁹ Environment Act 1990, section 94

Order or removing it. Whilst there is no requirement to remove the domestic Exclusion Order under the Regulation, the option of keeping it is problematic for several reasons. There are currently two separate provisions for vertical agreements under the Competition Act. In addition to the Exclusion Order, the EC Block Exemption Regulation⁹⁰ (BER) for vertical agreements has parallel effect in the UK by virtue of section 10 of the Competition Act⁹¹. Companies in the UK can therefore rely on the provisions of the BER to remove them from the scope of both the UK and EC regimes. The Government believes that the existence of two regimes under the Competition Act is potentially confusing for business.

2.5 In addition, now that the Competition Act has been in place for some time and both business and the competition authorities have more experience of how the Act is applied in practice, the Government believes it is right to review whether the Exclusion Order is the appropriate regulatory approach. The BER more precisely reflects current economic thinking on the treatment of vertical agreements between Member States. Vertical agreements are generally benign except where they are accompanied by market power. The terms of the BER reflect this approach more closely than the Exclusion Order.

2.6 Furthermore, the value of the domestic exclusion after modernisation will also be limited by the fact that the OFT will be under an obligation to apply Article 81 to the same agreement where there is an effect on inter-state trade and this will lead to an increased risk of conflict between the two

⁹⁰ 2790/99/EC Commission Regulation on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices

⁹¹ Section 10 provides that "an agreement is exempt from the Chapter I prohibition if it does not affect trade between Member States but otherwise falls within a category of agreements which is exempt from the Community prohibition by virtue of a Regulation."

legal frameworks. The Government's view is that the same authority will be treating similar agreements differently depending on whether they are caught by EC law or domestic law and that this is unfair. The Government believes that the better regulatory option is to remove the domestic Exclusion Order and to rely on the BER.

Competition Scrutiny Regime for Statutory Audit

2.7 Under the Companies Act, the Secretary of State has powers to formally "recognise" bodies authorised to ensure the proper training of registered auditors (Recognised Qualifying Bodies or RQBs) and to ensure the appropriate supervision of audit firms (Recognised Supervisory Bodies or RSBs). The Companies Act also provides for the Secretary of State to seek competition advice from the OFT before deciding whether to recognise a RSB or RQB. There is a corresponding exclusion from the Chapter I prohibition of the Competition Act for agreements and practices scrutinised under the separate regime in the Companies Act.

2.8 There are three options to be considered for the competition scrutiny regime for statutory audit: to retain it as it currently stands; to repeal it; or to amend it.

2.9 Retaining the regime as it stands is problematic for a number of reasons. The requirement for the OFT to apply Article 81 in any case where there is an effect in inter-state trade may result in OFT suspending scrutiny under the regimes in the Companies Act and considering the relevant rules, guidance and practice under Article 81 instead. The Government's preliminary view is that the rules and guidance of professional bodies in the accountancy sector may be caught by EC law and in light of this, the competition scrutiny regime in the Companies Act will fall into disuse after

the Regulation comes into force. In the Enterprise Act, Parliament repealed the regime providing special treatment for the professions in Schedule 4 to the Competition Act. It would not be consistent with the Government's policy of ensuring that the professions are fully within the scope of the Competition Act to retain the special scrutiny regime and corresponding exclusion for statutory audit.

2.10 The Government does not favour the option of amending the regime. The test under the provisions in the Companies Act is different from that which would be applied under the Competition Act or under Article 81 and 82 EC. Whilst this could be amended to include consideration of the rules, guidance and practices under Articles 81 and 82, it would not be possible to subsequently exclude the rules from the scope of EC law. Such scrutiny would also have to be applied with great care as the rules and guidance are initially considered before they have been put into operation rather than, as under the Competition Act and the Treaty Articles, once their effects are fully known.

2.11 The Government therefore favours the option of removing the scrutiny regime and corresponding exclusion.

Exclusion for agreements given prior clearance under section 21(2) of the Restrictive Practices Act

2.12 At the time of the Competition Bill, a large number of agreements existed which had been given prior clearance under section 21(2) of the Restrictive Trade Practices Act 1976 ('RTPA'). In order to smooth the transition between the competition regime under the RTPA and the prohibitions based approach of the Competition Act, the Government

provided an exclusion for such agreements. There are two options for the RTPA exclusion: either to keep it or to remove it.

2.13 The problems associated with keeping it are similar to those of the other exclusions discussed here. An agreement, which benefits from a section 21(2) direction excluding it from the Competition Act, may have an effect on inter-state trade. In this case the OFT will be required to look at the agreement under Articles 81 and 82 after modernisation and the domestic exclusion will be of limited value. The position may therefore be confusing for businesses with agreements that benefit from these clearances if the exclusion is kept. In any case this exclusion does not currently provide absolute legal certainty for undertakings. The OFT can issue a direction to withdraw the benefit of an exclusion by exercising a “claw back” and an agreement also ceases to be excluded if it is varied. We are seeking views on whether this exclusion should be removed.

3. COSTS AND BENEFITS

Business sectors affected

3.1 The Regulation will apply to all undertakings (broadly defined as organisations acting commercially) in the UK, provided that the agreement or behaviour in question may affect trade between EU Member States to an appreciable extent. It will thus tend to apply more to larger undertakings, but SMEs may occasionally be caught where they are significant players in niche markets.

3.2 However, the removal of these exclusions will not affect all undertakings. Businesses whose agreements or conduct affect trade between Member States do not currently benefit from these domestic

exclusions as they already have to comply with European competition law. Therefore the removal of these exclusions will only affect undertakings whose agreements or conduct *only* have an affect on trade within the UK. The European Court of Justice has adopted a wide definition of what may affect inter-state trade. As a result, large numbers of agreements and certain types of conduct of UK firms are already caught by Article 81 or 82.

Vertical Agreements

3.3 Vertical agreements may occur in almost any sector. However they are prevalent in the newspaper and magazine industry, the retail sector, broadcasting and media related sectors and sectors where franchising arrangements are common. The vast majority of vertical agreements are not restrictive of competition and will therefore not be prohibited. Removing the Exclusion Order and relying on the BER⁹² will still retain a “safe harbour” for the majority of UK vertical agreements.

3.4 Businesses which will need to consider their agreements anew will primarily be those whose agreements have no appreciable effect on trade between Member States but do have an appreciable effect on competition within the UK and whose market share falls above the threshold of the BER (30%) and below the threshold above which dominance is generally found under the Competition Act (40%)⁹³. Businesses whose agreements contain

⁹² The BER applies to the Chapter I prohibition by virtue of section 10 to the Competition Act

⁹³ The OFT considers it unlikely that an undertaking will be individually dominant if its market share is below 40%, although dominance could be established below that figure if other relevant factors provided strong evidence of dominance. Assessment of Market Power, OFT 415, September 1999, paragraph 2.11

any of the hard-core restrictions identified in the BER will also be affected⁹⁴. However, these agreements are exactly those that OFT might wish to claw back using its power under the Exclusion Order. It is also possible that networks of vertical agreements could be considered under market investigation powers in the Fair Trading Act 1973⁹⁵ so it is difficult to assess how many businesses will be affected by the removal of the Exclusion Order. We have spoken with both legal practitioners and the CBI and have been unable to establish estimates of numbers of businesses affected. However those businesses that are affected will incur costs arising from a need to seek legal advice on the status of their agreements following the removal of the Exclusion Order. Our initial estimates suggest that the costs of such legal advice might be of the order of £3,000 to £4,000 for an individual agreement but could be anywhere between £2,000 and £10,000 for a group of agreements depending on how many agreements are considered and whether they are similar in nature or not.

3.5 We would appreciate any further information on businesses which might fall into the category outlined above and will therefore be affected by the removal of the domestic verticals exclusion. We would particularly appreciate any information on the cost of legal advice that may be expended to evaluate the validity of agreements and the number of businesses likely to incur them.

⁹⁴ These hard-core restrictions are: resale price maintenance; restrictions concerning the territory into which or the customers to whom the buyer may sell; restrictions on the sales to end-users by authorized distributors in a selective distribution network; restrictions on authorized distributors in a selective distribution network selling or purchasing from other members of the network; and restrictions preventing the sale of components as spare parts by the manufacturer of the component to end-users, independent repairers and service providers.

⁹⁵ Shortly under provisions in the Enterprise Act 2002

Competition Scrutiny Regime for Statutory Audit

3.6 The bodies affected by the removal of the competition scrutiny regime under the Companies Act and related exclusion from the Competition Act are those currently “recognised” as RSBs or RQBs. These are the Association of Chartered Certified Accountants, Institute of Chartered Accountants in England and Wales, Institute of Chartered Accountants in Ireland, Institute of Chartered Accountants in Scotland, Association of International Accountants and the Association of Authorised Public Accountants. However, the removal of the regime does not mean that the rules, guidance and practices of the respective bodies are appreciably restrictive of competition law. The Government is also currently consulting on proposals to amend the regulatory structure of the audit profession. In view of this, it is not clear what the specific costs of removing the competition scrutiny regime might be. **We would appreciate any information on the cost of legal advice that may be expended to evaluate the validity of rules, guidance or practices of the accountancy bodies.**

Exclusion for agreements given prior clearance under section 21(2) of the Restrictive Practices Act

3.7 The removal of the RTPA exclusion will only affect those businesses which still have a valid agreement in operation that benefits from a direction under section 21(2) of the RTPA and has no effect on inter-state trade. Only these agreements are currently excluded from the Competition Act. At the time of the passage of the Competition Bill, thousands of these agreements were thought to be in existence although OFT had no precise data available. Many of these agreements may have been amended and will no longer benefit from the exclusion. Some may also have been replaced by new agreements which also do not benefit from the exclusion. We have not

therefore been able to establish how many agreements may still be in existence to which the removal of the exclusion would be directly relevant.

3.8 We would appreciate further information from undertakings whose agreements fall within this category in order to better inform our policy and the final RIA.

Benefits

3.9 The removal of these exclusions is designed to align more closely the scope of UK and EC competition law so as to avoid differential application of the law to similar agreements or conduct based on whether those agreements or conduct fall within one legal framework rather than another. Aligning the two systems more closely will result in one set of rules to follow instead of two and greater clarity and legal certainty for business and a lighter regulatory burden. It will also provide greater operational efficiency for national competition authorities. Not to align would create undesirable burdens on business and build in inefficiencies for the competition authorities.

Compliance cost for business

3.10 Implementation costs will mostly be associated with the introduction of the new “modernised” regime as a whole such as the need for staff training. We expect this burden would fall mainly on legal firms (and also lawyers employed by non-legal firms), many of which regularly consider issues of competition law and are engaged in programmes of continuous professional development. We therefore believe the costs to business generally should be relatively small.

3.11 We would appreciate further information from businesses which believe they will be affected by the removal of any of these exclusions and the likely costs they will incur (for example legal or administration costs).

4. ISSUES OF EQUITY AND FAIRNESS

4.1 As with all competition legislation, the Regulation and implementing SI address the inherent unfairness of consumers and businesses having to pay artificially high prices as the result of cartel activity or other anti-competitive acts. With very limited exceptions, the provisions of both the Regulation and the Competition Act apply to all businesses and organisations trading commercially; but only those that engage in anti-competitive practices falling within the scope of the prohibitions are at risk of investigation and sanctions.

4.2 Aligning the two systems addresses the inherent unfairness of different treatment being applied to similar agreements or conduct by UK companies depending on whether their agreements or conduct fall to be considered under EC law or not.

5. IMPACT ON SMALL BUSINESS

5.1 SMEs, like all undertakings, will potentially be affected by the removal of these exclusions if their agreements or conduct have an appreciable effect on trade within the UK (yet no effect on trade between Member States) and they fall into the categories identified in section 3 above. However, the OFT guidance "Assessment of Market Power" states that "an agreement will generally have no appreciable effect on competition if the parties' combined

market share of the relevant market does not exceed 25 per cent”⁹⁶ except where hardcore restrictions such as price fixing and market sharing are found in which case these will be considered to have an appreciable effect. An undertaking will not generally be found to be dominant if it has a market share of less than 40%, although in certain cases the threshold may be lower. SMEs only infrequently fall within competition law therefore.

5.2 In the case of the proposal to remove the Exclusion Order for vertical agreements and to rely on the BER, SMEs will mostly benefit from the protection offered by the BER unless their agreements contain one of the hard-core restrictions identified or unless they have a large share of a niche market or are party to an agreement with a larger firm whose market share exceeds the 30% threshold of the BER. Repealing the competition scrutiny regime for Statutory Audit and corresponding exclusion from the Competition Act is unlikely to have an adverse effect on small accountancy and audit businesses or on the small firms they serve. However, there may be SMEs whose agreements have been cleared under section 21(2) of the RTPA. They are unlikely to be affected by the removal of the exclusion from the Competition Act if they fall below the threshold at which such an agreement might have an appreciable effect on competition as described above in paragraph 5.1.

5.3 SMEs who infringe the Competition Act prohibitions are in any case protected from financial penalties if they fall below certain turnover

⁹⁶ Assessment of Market Power, OFT 415, September 1999, paragraph 2.3. See also: The Chapter I Prohibition, OFT 401, March 1999, paragraphs 2.19-2.20.

thresholds⁹⁷. The OFT may withdraw these immunities where hard-core restrictions such as price fixing are found.

5.4 We would welcome any further information from small businesses which believe they will be affected by the removal of these exclusions. Our current view is that very few will fall into the affected categories.

6. COMPETITION ASSESSMENT

6.1 The key aspect of the proposal to remove selected exclusions is to align, as far as possible, the treatment of agreements and conduct under the Competition Act with the treatment of equivalent agreements or conduct under Articles 81 and 82. This should result in clarity and simplicity of procedures, whether for the application of European or national competition law, which in turn will increase predictability for business. We do not believe that these changes will impact adversely on competition.

6.2 The proposal to repeal the Exclusion Order for vertical agreements and to remove the exclusion for agreements given clearance under the RTPA may improve competition by opening up some restrictive agreements to scrutiny and to third party action.

⁹⁷ Sections 39 and 40 of the Competition Act provide immunity from penalties for small agreements and conduct of minor significance respectively. The Competition Act 1998 (Small Agreements and Conduct of Minor Significance) Regulations 2000 defines the category of small agreements as being all agreements between undertakings, the combined applicable turnover of which does not exceed £20m in the business year preceding one in which the infringement occurred. Conduct of Minor Significance is defined as that by an undertaking, the applicable turnover of which, in the business year preceding one in which the infringement occurred, does not exceed £50m.

7. OTHER COSTS

7.1 The removal of these exclusions should not entail any significant increase in enforcement costs for UK competition authorities. Costs may arise in relation to the preparation of new guidance and investigating some new cases but these will be minimal. In the context of giving effect to the Regulation, we are currently consulting on amending the Competition Act to introduce a legal exception regime. Savings for the OFT will arise from ending notifications. The OFT estimate that the total additional costs of the new regime (including costs arising from the removal of these exclusions) should not exceed the savings.

8. CONSULTATION

8.1 In 1999, the DTI consulted representatives of businesses, lawyers and trade associations on the draft Exclusion Order for vertical agreements. At this point the scope of the EC block exemption was unknown and the UK opted to put its own exclusion in place to cover the interregnum between the Competition Act coming into force and the coming into force of the BER⁹⁸, so as to avoid precautionary notifications of large numbers of essentially benign agreements. However, many of the respondents to the consultation suggested that it was sensible to align closely with the European regime. This is what we are now proposing.

8.2 In 2001, the proposal to repeal the Exclusion Order for vertical agreements exclusion was put forward in the “Productivity and Enterprise”

⁹⁸ March 2000 and June 2000 respectively

white paper⁹⁹. The responses to the White paper in 2001 were varied. Slightly less than half the respondents commented on the proposal. Of those that did (30), responses were almost evenly split between those endorsing removal and those opposing it. One concern that was raised was that OFT would be flooded with notifications of vertical agreements if the exclusion were removed. The Government is currently consulting on replacing the notification system with a legal exception regime.

8.3 In considering these previous responses it is important to note that the situation has changed since 1999. The Competition Act has now been in force for 3 years and few notifications have been made to OFT. Businesses have a better understanding of how the regime works and are much better placed to decide whether their agreements are legal or not. Regulation 1/2003 changes the position again by transferring powers to apply EC law from a more remote Commission to our domestic competition authorities. This is one of the reasons the Government is reviewing the Exclusion Order for vertical agreements.

8.4 Informal consultation on the proposals to remove some of the domestic exclusions from the Competition Act has been undertaken with other Government departments including the OFT and with selected businesses and trade associations. Our policy position has been reached in agreement with these departments.

8.5 Due to the time needed to bring the Statutory Instrument into force on 1st May 2004 (to coincide with the application of the Regulation) the consultation period for this proposal is eight weeks. This will allow the

⁹⁹ "Productivity and Enterprise – A World Class Competition Regime" Cm5233. Available on-line at <http://www.dti.gov.uk/ccp/topics2/ukcompref.htm>

Government to publish a response to both this consultation and the previous one on the main proposals following modernisation along with a draft Statutory Instrument in September 2003. To compensate for the curtailed consultation period, we will be holding workshops with interested parties to discuss the proposals in detail and will welcome further comments when the draft Statutory Instrument is published in the Autumn.

9. SUMMARY & RECOMMENDATIONS

9.1 Given the arguments set out in this RIA, the Government believes that removing these exclusions will contribute to establishing a new regime which will benefit UK business overall and strengthen the Single Market. Decentralising enforcement of EU competition rules and focussing it on serious infringements, providing a common competition standard for industrial co-operation across the EU, and reducing bureaucracy on enforcers and on business, will contribute to more effective competition in the Single Market.

9.2 Equally, producing, as far as possible, a unitary set of procedures and sanctions irrespective of which legal base is being deployed will benefit business by creating greater consistency and clarity and by reducing the costs of legal advice. It will also foster greater efficiency and effectiveness in enforcing competition law by NCAs.

10. ENFORCEMENT, SANCTIONS & REVIEW

10.1 The Regulation obliges national competition authorities to apply Articles 81 and 82 and empowers national courts to hear Articles 81 and 82

cases. Therefore enforcement of the new regime in the UK will fall to the OFT (and the sectoral regulators) and national courts as well as the Commission and Community courts. However, the Regulation leaves it to national law to determine the appropriate sanctions for Article 81 or 82 infringements and we are consulting on what the maximum penalty should be¹⁰⁰.

10.2 The Regulation includes a requirement for the Commission to report to the European Parliament and the Council on the functioning of the regulation five years after it comes into force (i.e. 1st May 2009). The emphasis of the report will be on how well the Commission's power to initiate proceedings relates to the use by NCAs of their powers to apply Articles 81 and 82¹⁰¹, and on the functioning of the Commission's power to investigate sectors of the economy and types of agreements¹⁰². On the basis of this report the Commission will decide whether it would be appropriate to propose revisions of the Regulation to the Council.

10.3 The UK Competition Act has been reviewed in the course of both this work and the development of the Enterprise Act. It will be subject to a further review in the second half of 2007, three years after the statutory instrument implementing modernisation comes into force.

¹⁰⁰ UK Competition Law – Modernisation – A consultation on the Government's proposals for giving effect to Regulation 1/2003 EC and for re-alignment of the Competition Act 1998, April 2003, URN 03/750

¹⁰¹ The Regulation, Article 11(6)

¹⁰² The Regulation, Article 17

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 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 Mr P Martin, DTI Consultation Co-ordinator, Room 725, 1 Victoria Street, London SW1H 0ET or telephone him on 020 7215 6206 or email philip.martin@dti.gsi.gov.uk.

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