Tightening the System: The Nature and Likely Effect of UK Competition Reforms

BY GREG OLSEN AND DANIEL HARRISON

ON MARCH 15, 2012, THE DEPARTMENT of Business, Innovation and Skills of the UK government announced reforms of the country's competition laws and the structure for enforcing those laws.[1] They amount to the most substantial change to the UK competition landscape since price fixing was criminalized a decade ago.

The most notable change is institutional. The UK's two primary enforcers of competition law—the Office of Fair Trading (OFT) and the Competition Commission (CC)—will be replaced by a single Competition and Markets Authority (CMA), which is intended to be operational by April 2014.

The government also announced various changes to the different regimes that make up UK competition law: the civil regime for enforcement of the prohibitions on anticompetitive agreements and abuse of dominance under the Competition Act 1998 and the Treaty on the Functioning of the EU (TFEU);[2] the criminal regime for prosecution of cartel conduct; the merger control regime; the regime for market-wide investigations; and various sector specific regulatory regimes. One change that has drawn much attention is the removal of the requirement to prove dishonesty to secure a criminal conviction for participation in a cartel, but there will also be material changes in other areas, such as the introduction of binding deadlines for the conclusion of Phase 1 merger control reviews.

While the reforms are substantial, they are not as radical as they could have been. The government consulted on wide-ranging proposals, including mandatory filing and standstill obligations for the merger control regime and a prosecutorial model whereby breaches of the civil prohibitions on anticompetitive agreements and abuse of dominance would be decided by a court in the first instance, instead of by the CMA.[3] These were abandoned in the face of strong opposition from business representatives and practitioners (to the merger proposals),[4] and the existing authorities (to the civil enforcement proposals).[5]

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A New, Single Agency

The merger of the OFT and the CC is intended to allow more flexible and efficient use of competition powers and processes. At present, the authorities share competence in the areas of merger review and market investigations, with the OFT carrying out initial "Phase 1" assessments and, if the OFT refers a matter to it, the CC conducting a detailed "Phase 2" inquiry. With a single agency, parties subject to such investigations are likely to be relieved of the frustrations of having to explain issues and market dynamics to entirely separate Phase 1 and 2 case teams, as they do at present.[6] Conversely, however, they will also be deprived of the opportunity to make their case afresh to a case team untainted by potential "confirmation bias," i.e., an interest in seeing initial concerns confirmed in the eventual decision.

Weighing those advantages and disadvantages, the merger should, on balance, be positive for businesses operating or making acquisitions in the UK. In particular, the risks of confirmation bias will be mitigated in the areas of merger control and market investigations by the continued use of panels of independent experts—drawn from the business, legal, and academic communities—to decide upon Phase 2 matters.[7]

However, the merger will come in the wake of significant budget cuts of recent years, including a reduction in the OFT's budget of 25 percent (adjusted for inflation), phased over four years from 2011.[8] Achieving the necessary integration of functions without any further impact on the regulators' ability to recruit and retain high quality staff and focus resources on front-line enforcement activities, will be a challenge. In that context, strong leadership will be important. While the government has decided on the governance structures for the CMA,[9] it has yet to announce who will be Chief Executive Officer. One of the strongest candidates for that position—John Fingleton, the current Chief Executive of the OFT—appears to have ruled himself out by announcing that he will leave the OFT later this year.[10]

Merger Control

Merger filings in the UK will remain voluntary, and parties will not be subject to an automatic "standstill" obligation in Phase 1, prohibiting closing prior to clearance or the expiry of any waiting period.[11]

The mergers regime has not escaped change altogether, however. In particular, fees will increase sharply from October 6, 2012, with the largest deals—in which the target has turnover in the UK of at least £120 million (approximately $190 million)—subject to a filing fee of £160,000 (approximately $250,000).[12] That puts maximum UK filing fees as second only to those of the United States, where a maximum fee of $280,000 may be payable. Indeed, the UK arguably will become the jurisdiction with the world's highest average filing fees per transaction reviewed, when it is considered that the maximum U.S. fee kicks in only at a much higher deal value threshold (when assets or voting securities of more than $682 million are involved).[13] Moreover, the minimum filing fee in the UK—£40,000 (around $64,000), which applies where the target has a UK turnover anywhere below £20 million (around $32 million)—is substantially higher than the minimum filing fee in the United States ($45,000, for transactions involving securities or assets valued at less than $136.4 million).[14] Other than the United States, very few regimes in the world have a *maximum* filing fee, at current exchange rates, in excess of the *minimum* £40,000 fee that will apply in the UK.[15]

While automatic standstill obligations were not introduced, the CMA will have new powers to require parties that have closed their mergers to reverse, for the duration of the review process, any steps already taken to integrate their respective businesses. These will be in addition to existing powers to require parties to hold their respective businesses separate from each other and to maintain them as appropriately-resourced market players pending review. Such obligations can prove extremely costly for those that take the risk of closing without first obtaining clearance.

The reforms will also impose binding deadlines of forty working days from filing for Phase 1 decisions, which will replace the current system of non-binding administrative deadlines and a rarely used option to trigger a binding statutory timetable.[16] For complex cases, however, the CMA may not be able to deal with all the issues within this timeframe, potentially creating an increased risk of a Phase 2 investigation to allow the CMA to complete its assessment. However, it is considered more likely that in such cases the overall period within which the merging parties are engaged with the CMA will be broadly unchanged, but with longer pre-notification discussions and use of the CMA's power to "stop the clock" during the Phase 1 review period, while awaiting information that it has requested from the parties.[17]

The reforms will also introduce binding timetables for the formulation of remedies in Phase 1 (fifty working days, which can be extended to ninety working days in certain circumstances) and Phase 2 (twelve weeks, with a possible six-week extension). In contrast to the present system in which parties must offer Phase 1 remedies before the OFT has come to any firm conclusions regarding the effects of the merger, under the new regime, parties will have a statutory five working day period from receipt of the CMA's decision that it intends to commence a Phase 2 inquiry within which to offer remedies with a view to avoiding that fate. The parties and CMA will then have a further forty-five working day period (which can be extended yet further by forty working days in certain circumstances)[18] to consider, negotiate, and finalize remedies. At ninety working days from the Phase 1 decision, the maximum Phase 1 remedies process will be the same duration as many Phase 2 proceedings, such as those under the EU Merger Regulation. The new regime, however, does have the advantage of flexibility, such that remedies necessitating the signing of an agreement with an upfront buyer for the sale of a divestment asset will remain much more viable than they are, for instance, during Phase 1 proceedings before the European Commission.

Criminal Antitrust Enforcement

In the UK, the legislation which criminalizes cartel conduct (the Enterprise Act 2002) is separate from that which imposes civil penalties for anticompetitive agreements (the Competition Act 1998).[19] This is in contrast to the United States, for example, where a breach of a single legislative provision—Section 1 of the Sherman Act—can result in criminal or civil penalties. This duality of regimes created some difficulties for the legislature when it came to define the scope of the criminal offense. In particular, how could it be framed in such a way that it focuses on the most "wrongful" antitrust breaches, excluding all conduct that would not breach the separate civil prohibitions, while obviating the need for juries to consider complex evidence regarding the economic effects of a particular arrangement?

The solution in the Enterprise Act 2002 is a requirement that prosecutors prove that an individual had "dishonestly" agreed with another to fix prices, restrict output, share markets or customers, or engage in bid rigging. Ten years later, no jury has had the opportunity to decide whether an individual entered into a cartel arrangement with dishonesty, as no trial has proceeded to that stage.[20] The OFT (the body that currently has the main responsibility for prosecuting the cartel offense) attributes this paucity of cases in part to the perceived difficulty of persuading a UK jury of a defendant's dishonesty. Businesses and practitioners point to different reasons, such as a high level of antitrust compliance, and investigative failings on the part of the OFT. In any event, in reforming the competition laws, the government accepted the OFT's position, and so has decided to abolish the requirement to prove dishonesty. One of its stated reasons is to increase the number of prosecutions to a (seemingly arbitrary) level that had been envisaged when the criminal offense was created.

In place of the dishonesty criterion will be an exception for

agreements made "openly," i.e., there will be no breach if the parties intended, at the time they entered into the relevant price-fixing, market sharing, or bid-rigging arrangements, to publish salient details in a suitable publication. The government refers to the *London Gazette*—an official newspaper for legal and regulatory announcements—as an example of such a publication.[21]

The new offense, as currently proposed, gives rise to a number of difficult issues, which will need to be addressed during the legislative process or in administrative guidance. In particular, it is unclear what businesses will need to do with respect to the categories of agreements that fall within the legislative definition of price fixing or market sharing but are nonetheless benign from a competition perspective. For example, under EU law automatic "block" exemptions from the civil prohibition on anticompetitive agreements are available for arrangements whereby a producer agrees to share geographic markets or customers with a distributor,[22] and for certain forms of price fixing that occur within the context of a production joint venture.[23] The *London Gazette* will become an unusually weighty publication if every such arrangement must be advertised in it, yet that appears to be the implication of the planned reform. Moreover, while publication need not occur until just before the parties plan to implement an arrangement, and need not contain all details of the relevant contracts, it seems likely that the new law will create conflicts of interest between employees—who will push for precautionary publication of anything that could conceivably fall into the category of cartel conduct—and their employing companies, for which the maintenance of business confidentiality may be a greater concern.

The government contends that the offense will contain the requisite intent element (mens rea), as it will still be necessary to show that the individual intended to enter into the agreement in question, even if it is no longer necessary to show that the individual knew or ought to have known that the agreement was a dishonest one.[24] In that sense, the position in the UK will become more closely aligned with that of the United States, where the mens rea requirement for a criminal antitrust offense can be established by proving knowing participation in a per se illegal conspiracy without the need for proof of intent to produce anticompetitive effects.[25] Unlike in the United States, however, the UK criminal offense is not supplemented by established lines of case law that carefully circumscribe what constitutes per se infringement. Consequently, businesses that engage in benign arrangements that fall within the legal definition of price fixing, market sharing, and bid rigging, and which inadvertently fail to publish those arrangements, will be reliant on courts and prosecutors to adopt a practical and purposive interpretation of the law. It will also become even more important that employees are carefully trained in what they may and may not do when communicating with competitors, with a focus on examples that are more ambiguous than straightforward price fixing in a smoke-filled room.

Civil Antitrust Enforcement

The Government had mooted the possibility of withholding from the CMA decision-making powers for civil infringements of the Competition Act 1998 and Articles 101 and 102 TFEU and conferring them upon a court, with CMA officials litigating the case in much the same way as the OFT currently pursues a criminal offense. The reasoning was that, because the majority of civil infringement findings of the OFT are appealed to the UK's specialist antitrust court—the Competition Appeal Tribunal (CAT)—allowing the CAT to rule on infringements in the first place would save time. Such a decision-making structure also would have addressed due process concerns voiced by many that combining case selection, investigation, and decision making within the same authority creates significant concerns with respect to due process and confirmation bias.[26]

However, reactions to the government's proposal were mixed, and the OFT in particular was strongly opposed to it.[27] As a result, the government instead asked the OFT to further refine and improve its current procedures, with a view to taking more cases forward and taking decisions that are more "robust" (i.e., less susceptible to successful appeal). On March 28, 2012, the OFT published its proposals for meeting that challenge, with a new decision-making structure involving a move to collective judgment, and the separation of the decision makers from the investigation team.[28]

The OFT's proposed changes include the publication of case opening notices and administrative timetables, more "state of play" meetings between the parties and investigating officials, a new ability for parties to make representations on key elements of draft penalty calculations, enhanced oral hearings, and new arrangements for internal checks and balances.[29] The OFT also announced an extension of its trial of a "Procedural Adjudicator"—an OFT official who acts as an initial referee in procedural disputes between the investigating case team and the parties under investigation—for another year, with an expanded mandate.[30]

For its part, the government will legislate a number of statutory procedural rules, setting out a principle of separation of decision making from investigation. The new rules also will modify the civil antitrust regime, including by granting new powers for the CMA to conduct compulsory oral interviews, imposing civil penalties for non-compliance with its requests and decisions, and setting lower thresholds for the imposition of interim measures by the CMA.[31]

Market Investigations

The UK market investigation regime is unusual, in that it allows the UK's competition authorities not only to investigate competition within a particular sector or market, but also to impose remedies—including divestments, price controls, and injunctions[32]—to address any features that they consider to have an adverse effect on competition in the UK, without needing to have recourse to any legislative procedure and with only limited[33] democratic or parliamentary account-

ability.[34] Companies operating in an investigated market thus can find themselves subject to far-reaching and costly remedies (at the end of a wide-ranging and expensive investigation process) despite the absence of any suggestion that they have infringed any law. Given this, many businesses consider that *any* use of the market investigation regime is more interventionist than can be justified.[35] The UK government, however, takes the opposite view: that the regime is "at the forefront of global best practice" and is currently "underutilized," by reference to (again, seemingly arbitrary) initial anticipations of four market investigation references per year.[36]

Accordingly, the net will be cast even more widely, with the CMA acquiring new powers to report on cross-market practices and public interest issues.[37] The government identified below-cost selling and consumer switching costs as two examples of such cross-market issues.[38] One hopes that any cross-market inquiries that are launched identify issues that are more narrowly defined.

More frequent consideration of public interest issues[39] has the potential to cause substantial legal uncertainty for businesses. This is not just because the government is likely to retain the power to define what is in the public interest after the fact,[40] but also because the scope of conduct that can be called into question is so wide. For example, when public interest issues are raised in the merger regime, the question is whether the *transaction in question* might adversely affect the public interest.[41] In the new market regime it will be whether *any* conduct of businesses in a given sector might do so.[42] In addition to covering a broad range of activity, this move also runs the risk of re-politicizing a regime which previous reforms were at pains to de-politicize.

In terms of procedure, the existing distinction between preliminary Phase 1 market "studies" and in-depth Phase 2 market "investigations" will remain, with the latter being decided upon by independent panels within the CMA.[43] The announced reforms will introduce:

- binding time limits and information-gathering powers during Phase 1 studies (these will require the CMA to consult on launching a Phase 2 investigation within six months of launching a market study, where such an outcome is envisaged, and to conclude all market studies within twelve months);[44]
- a reduction of the binding time limit for Phase 2 investigations from twenty-four months to eighteen months, subject to a possible six-month extension in exceptional circumstances;[45] and
- a new six month deadline from the CMA's final report for implementation of Phase 2 remedies, subject to a possible extension of four months.[46]

Enforcement of Competition Law by Sector Regulators

The UK has numerous sector regulators with authority to enforce the civil prohibitions on anticompetitive agreements and abuse of dominance in their respective industry sectors, concurrent with the OFT's exercise of those powers, and in addition to powers that they exercise under sector specific regulatory regimes (such as licensing regimes).[47] The government has decided that these regulators will retain their concurrent powers, but will become subject to strengthened obligations to consider the use of their competition powers before using regulatory powers. The CMA will also be empowered to intervene in civil competition investigations that are carried out by sector regulators where it is "better placed" to act, although there is not yet any guidance on when those circumstances may arise.[48]

Timing

The reforms are subject to Parliamentary timing and approval. The government has stated that its aim is to have the CMA operational by April 2014, and has stated that it will introduce draft legislation (the Enterprise Bill) to the UK Parliament in the Parliamentary session that started on May 8, 2012.[49]

Conclusion

The reforms were initially billed as a move to rationalize the institutional structures of the UK's enforcement agencies, but the scope of the government's considerations was ultimately expanded to cover almost every aspect of the enforcement of competition law in the UK. Some of the proposed reforms—such as the removal of the requirement to prove dishonesty in criminal cases—appear to have been motivated by a desire for more enforcement, by reference to preconceived ideas of how many cases per year should be brought.

On balance, while there will no doubt be transitional issues arising from the institutional upheaval involved in the merger of the OFT and the CC, the announced reforms should not, in themselves, create a significant risk that the quality of decision making will be adversely impacted. Some of the more radical changes under consideration could have exacerbated that risk greatly, so in this respect the final reforms are to be welcomed. ■

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[1] Dep't for Bus., Innovation and Skills: Growth, Competition and the Competition Regime: Government Response to Consultation (2012) [hereinafter Government Response to Consultation], *available at* http://www.bis.gov.uk/assets/biscore/consumer-issues/docs/g/12-512-growth-and-competition-regime-government-response.pdf.

[2] Consolidated Version of the Treaty on the Functioning of the European Union, Sept. 5, 2008, 2008 O.J. (C 115) 47 (effective Dec. 1, 2009), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:0047:0200:en:PDF.

[3] Dep't for Bus., Innovation and Skills: A Competition Regime for Growth: A Consultation on Options for Reform (2011), *available at* http://www.bis.gov.uk/assets/biscore/consumer-issues/docs/c/11-657-competition-regime-for-growth-consultation.pdf.

[4] *See* Confederation of British Industries (CBI), Options for Reform of the Competition Regime: CBI Response to the BIS Consultation (2011) [hereinafter CBI Response], *available at* http://www.cbi.org.uk/media-centre/press-releases/2011/06/competition-regime-must-free-up-compa-

nies-to-invest-and-grow-cbi/; The City of London Law Society Competition Law Committee, Response to BIS Consultation on Reforming UK Competition Regime (2011) [hereinafter City of Londn Law Society Response], *available at* http://www.citysolicitors.org.uk/FileServer.aspx?oID=1030&lID=0.

[5] OFT, A Competition Regime for Growth: A Consultation on Options for Reform, The OFT's Response to the Government's Consultation (2011) [hereinafter OFT's Response to the Government's Consultation], *available at* http://www.oft.gov.uk/shared_oft/consultations/OFT1335.pdf.

[6] It will be for the CMA, when constituted, to decide whether case teams will flow, in whole or in part, from Phase 1 to Phase 2. However, in light of the operational efficiencies that it would achieve, some degree of "flow through" is considered likely.

[7] Government Response to Consultation, *supra* note 1.

[8] OFT, Annual Report and Accounts 2010–11 (2011), *available at* http://www.oft.gov.uk/shared_oft/annual_report/2011/annual-report-10-11.pdf.

[9] The CMA Board will have responsibility for strategy, performance, rules and guidance, and for Phase 1 merger and market investigation decisions (governance structures in respect of antitrust decisions have yet to be finalized). The Board will comprise a non-executive Chair, a Chief Executive Officer, a number of executives (likely to be 2 or 3), and a number of non-executives (likely to be 4 or 5). Government Response to Consultation, *supra* note 1.

[10] Press Release, OFT, OFT Chief to Step Down Later This Year (2012), *available at* http://www.oft.gov.uk/news-and-updates/press/2012/10-12.

[11] Currently, standstill obligations apply once a Phase 2 investigation by the Competition Commission is initiated (under sections 77 and 78 of the Enterprise Act 2002). The government has not announced any plans to change this feature of the merger control regime.

[12] Government Response to Consultation, *supra* note 1.

[13] Federal Trade Comm'n, Filing Fee Information, Feb. 27, 2012, *available at* http://www.ftc.gov/bc/hsr/filing2.shtm.

[14] *Id.*

[15] In Germany a fee of €100,000 is possible, but only in cases of exceptional complexity and economic significance. In Spain a maximum filing fee of €109,860 applies for transactions involving parties with a combined turnover of more than €21 billion in Spain.

[16] There will be no change to the Phase 2 timetable of twenty-four weeks, with a possible eight-week extension in exceptional circumstances. *See* Government Response to Consultation, *supra* note 1.

[17] The CMA will have information gathering powers during Phase 1 merger reviews that are not available to the OFT under the present regime. *See id.*

[18] Such as where the CMA requires an up-front buyer to be identified for a divestment asset.

[19] This is mainly because the civil prohibition in the Competition Act 1998 is largely identical to the prohibition under Article 101 TFEU, which also applies in the UK. Criminal penalties cannot be imposed for breaches of the Article 101 prohibition. The UK legislature therefore sought to create a clear distinction between the civil and criminal prohibitions under UK legislation, notwithstanding that they both apply to cartel conduct.

[20] Executives have been sentenced to prison under the Enterprise Act 2002 (for their part in a marine hoses cartel), but that was as a result of a plea bargain with the U.S. Department of Justice that required a guilty plea in the UK. *See* R. v. Whittle, 2009, U.K.C.L.R. 247. The only other trial (of a number of British Airways executives, for alleged fixing fuel surcharges) was abandoned by the OFT after evidentiary and procedural failings came to light. For a description of the events leading up to the trial's abandonment, see Julian Joshua, *Shooting the Messenger: Does the UK Criminal Cartel Offense Have a Future?*, Antitrust Source, Aug. 2010, at 1, http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Aug10_Joshua8_2f.authcheckdam.pdf; Mark Furse, *The Cartel Offence—"Great For A Headline But Not Much Else"?*, 32 Eur. Competition L. Rev. 223 (2011); OFT, Project Condor Board Review (2010), *available at* http://www.oft.gov.uk/shared_oft/board/2010/Project_Condor_Board_Review.pdf.

[21] Government Response to Consultation, *supra* note 1.

[22] Commission Regulation (EU) No. 330/2010, 2010 O.J. (L 102) 1, 3 (block exemption under Article 101(3) TFEU of certain categories of vertical agreements and concerted practices).

[23] Commission Regulation (EU) No 1218/2010, 2010 O.J. (L 335) 43, 46 (block exemption under Article 101(3) TFEU of certain categories of specialization agreements).

[24] Government Response to Consultation, *supra* note 1.

[25] United States v. Brown, 936 F.2d 1042, 1046 (9th Cir. 1991).

[26] *See* City of London Law Society Response, *supra* note 4.

[27] OFT's Response to the Government's Consultation, *supra* note 5.

[28] OFT, Review of the OFT's Investigation Procedures in Competition Cases—A Consultation Document (2012), *available at* http://www.oft.gov.uk/shared_oft/policy/OFT1263con2.

[29] *Id.*

[30] *Id.*

[31] Government Response to Consultation, *supra* note 1.

[32] The CC's remedy powers are set out in Schedule 8 of the Enterprise Act 2002.

[33] The Council of the Competition Commission is, in principle, accountable to the Secretary for Business, Innovation and Skills who is, in turn, accountable to Parliament for its actions. Competition Commission, Framework Document (2010), ¶ 2.8, *available at* http://www.competition-commission.org.uk/assets/competitioncommission/docs/pdf/non-inquiry/our_role/ms_and_fm/pdf/model_framework_document.pdf. In addition, members of the Council can be called to give an account of their actions to Parliament, e.g., before a Parliamentary "select committee." However, the CC is ultimately an independent regulator. Its remedy orders are not required to be laid before Parliament (Schedule 10, Enterprise Act 2002) and individual decisions are rarely, if ever, called into question through Parliamentary mechanisms. Moreover, the Secretary of State can intervene in the CC's decision-making only in the limited circumstances set out in the Enterprise Act 2002, and can remove its members only on grounds of incapacity or misbehavior. Schedule 7, ¶ 6(4), Competition Act 1998.

[34] The only other regime identified by the UK government with these features is that of Israel. Government Response to Consultation, *supra* note 1.

[35] *See* CBI Response, *supra* note 4

[36] Government Response to Consultation, *supra* note 1.

[37] *Id.*

[38] *Id.*

[39] The announced changes will not expand the scope of public interest considerations that may be taken into account under the market regime. Moreover, it will remain the case that the final decision on matters of public interest is taken by a government minister (the Secretary of State for Business, Innovation and Skills). However, the reforms will empower the Secretary of State to order the CMA to report on its recommendations on the relevant matters of public interest. The availability of such reports is likely to mean that in the future, Secretaries of State are more willing to intervene in market investigations on public interest issues than they have been in the past.

[40] It currently has the power to do so under sections 139(5) and (6) and 153(4) of the Enterprise Act 2002.

[41] Sections 45 and 54 of the Enterprise Act 2002.

[42] Government Response to Consultation, *supra* note 1.

[43] *Id.*

[44] *Id.*

[45] *Id.*

[46] *Id.*

[47] These are: The Office of Gas and Electricity Markets (OFGEM); The Office of Communications (OFCOM); The Water Services Regulation Authority (OFWAT); The Office of Rail Regulation (ORR); the Civil Aviation Authority (CAA); and the Utility Regulator for Northern Ireland (OFREG).

[48] Government Response to Consultation, *supra* note 1.

[49] *Id.*