The UK's new merger regime

A look at how things have changed

by ***Alastair Mordaunt****

The Competition and Markets Authority (the CMA) opened its doors to business on 1 April 2014. This article focuses on the new regime in relation to merger control, recalling the government's original rationale for making changes to the regime, identifying those changes and assessing their likely impact on merging parties.

Government's concerns about the regime

During its consultation for reforming the UK's competition regime, the government noted the merger regime as one of its key strengths but considered that there was further scope for improvement by addressing the disadvantages of the voluntary notification regime. The government noted two specific drawbacks with the system: "First, a risk that some anticompetitive mergers escape review. Second, it leads to the investigation of a large proportion of completed cases, which in turn makes it difficult to apply appropriate remedies in the event that they are found to be anticompetitive" (*A Competition regime for growth: a consultation on options for reform*, March 2011, p 33).

The government also noted that the regime could be speeded up and made more streamlined.

Key changes to the UK merger regime

The key changes introduced by the Enterprise Regulatory Reform Act 2013 include:

- a new binding 40 working day review deadline for Phase I mergers;
- a new remedy procedure at Phase I to follow the CMA's 40 working day review in cases where it has identified a substantial lessening of competition;
- new binding timetables for the formulation of remedies at Phase I (50 working days with a possible 40 working day extension) and Phase II (12 weeks with a possible six week extension);
- an enhanced hold-separate regime, including the ability at Phase I to suspend all integration steps in anticipated mergers before clearance, to ban completion of anticipated mergers and to reverse integration steps that have already taken place;
- new information-gathering powers at Phase I (equivalent to those that previously only existed with the UK Competition Commission at Phase II); and
- a new merger notice for notifying mergers to the CMA with extensive information provision requirements.

Following consultation on draft guidance to accompany these changes, the CMA made a number of welcome changes in its finalised guidance which it published in January, including:

- confirmation that, where practicable, merging parties would have access to the Phase I decision-maker at issues meetings; and
- clarification that the CMA will adopt a reasonable approach to assessing what type of information will be required in the new merger notice.

Will the review process be quicker?

Probably not.

In spite of the new binding 40 working day deadline, the CMA still has the ability to stop the clock when information is outstanding from merging parties. In addition, the CMA strongly encourages merging parties to engage in prenotification discussions with it at least two weeks before the intended date for notification. Given that the CMA has considerable discretion in determining when a party's merger notification is complete – and therefore when the clock starts running on the 40 working day deadline – it is expected that prenotification discussions will take place in most cases.

In addition, the new notification form – which is much more extensive than the European Commission's Form CO - may result in longer prenotification as a result of waiver discussions between the merging parties and the CMA.

In light of these changes, it is not at all clear that the Phase I process will speed up: in fact, the formal review period may not change significantly (because the CMA may still stop the clock) and overall "face time" with the authority might even increase (due to prenotification discussions).

On a more positive note, the binding timetables at the remedies stages of Phase I and II provide more structure and certainty for merging parties and should help to foster a more effective remedies system. One possible drawback might be that certain types of cases may be less amenable to a Phase I remedy outcome in the future. For example, a case involving multiple local divestments subject to the upfront buyer requirement may struggle to be completed within the new Phase I remedy timetable. Acquirers could try to mitigate this risk through increasing the amount of early work on remedies, although this can be difficult in practice when the focus of the company's attention is on demonstrating to the CMA why the merger does not raise concerns in the first place.

Will there be fewer or more references?

Possibly more.

The CMA's new information-gathering powers at Phase I will enable it to obtain evidence from third parties that it may not have previously been able to get. This power is good news (assuming it is used proportionately) as it may enable the CMA to resolve cases at Phase I that the Office of Fair Trading would previously have referred to Phase II. It remains to be seen, however, how many cases will fall into this category.

Perhaps more relevant is the potential loss of flexibility at

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Phase I that will result from the new binding timetable. On the one hand, merging parties now benefit from greater certainty regarding the review timetable. On the other hand, the CMA may lose some of the flexibility that the OFT had in those cases where a Phase I outcome was achievable by extending its administrative timetable by a short period of time. Under the new regime, the CMA is under a duty to refer a case on expiry of its 40 working day timetable where a substantial lessening of competition is identified unless one of the exceptions to the duty to refer is met.

It is possible that the increased use of prenotification discussions will mitigate this lack of flexibility on the timing of the CMA's Phase I decision. As in the EU, merging parties may enter into prolonged prenotification discussions to give themselves the best opportunity of obtaining a Phase I outcome and avoiding a long and costly Phase II review. Nonetheless, it is often difficult to predict each and every issue during prenotification and so flexibility at the start of the process may not entirely make up for a lack of flexibility at the end of Phase I.

In addition, it is conceivable that the CMA may decide to take a more holistic approach to merger control, now that both phases of review reside within the same organisation. Whereas, in the past, the OFT has gone the extra mile (so-called "Phase 1.5") in appropriate cases to obtain a Phase I outcome, the CMA may be more inclined to decide early on that certain cases are more amenable to an in-depth Phase II review and refer them, following a less detailed review at Phase I.

The impact of an increase in Phase II reviews for business could be mitigated if the CMA were to cut short its Phase II review in appropriate cases – for example, by sidestepping the provisional findings stage and going straight to a clearance decision or discussion of remedies – as the European Commission will sometimes do. However, the UK Competition Commission did not adopt such a policy (it would always issue provisional findings, for example) and there has been no indication that the CMA is considering changing policy in this respect. (Note, the CMA can pause its Phase II review in non-completed merger cases where the merging parties are considering abandoning their transaction altogether.)

Will the changes impact on incentives to notify?

Possibly yes.

Previously, a key benefit of the UK's merger regime was the ability not to notify a deal that fell within the OFT's jurisdiction and to close.

Notwithstanding the voluntary nature of the regime, there were certain risks of not filing or of closing and then filing. First, the OFT had the ability to call in non-notified mergers. Second, the OFT and CC had hold-separate powers that could, in practice, be extremely burdensome and costly (for instance, they can delay any merger synergies). Third, the CC ultimately had the power to prohibit a transaction which, if required, entailed reversing any prior integration. For these reasons, merging parties would consider carefully whether or not to notify the OFT voluntarily.

Under the new regime, the CMA has enhanced hold-separate powers; in particular, it has the ability at Phase I to impose hold-separate orders on non-completed deals, which may include prohibiting closing, and to reverse any integration steps that have already taken place. In addition, merging parties can no longer offer hold-separate undertakings but will instead have hold-separate orders imposed on them. The rationale is that this reduces the risk of pre-emptive integration, because it allows for obligations to be imposed quickly, without spending time on negotiating the terms of the undertakings.

Merging parties must now take these enhanced powers into account when deciding whether or not to notify, and it is possible that they will be more inclined to notify (and in so doing obtain greater legal certainty) than under the old regime. As a result, filing numbers may increase under the new regime. However, steep filing fees will continue to make legal certainty an expensive commodity.

Concluding remarks

The UK's merger regime is well respected and admired at home and abroad. While somewhat unique, the voluntary nature of the regime is considered by many as a strength – in that it enables a large proportion of relevant M&A transaction activity to bypass the regime altogether and does not prohibit completion (at least, not at Phase I) for the relatively small number of transactions that fall for investigation. The government's decision to retain the voluntary nature of the regime is therefore to be welcomed.

However, some potential concerns remain, particularly when bearing in mind the government's rationale for these changes.

First, it is not clear whether cases at Phase I will speed up in practice and, further, it is possible that the introduction of a prescriptive merger notice will increase information burdens on business unnecessarily. If correct, these impacts would run counter to the government's objective of speeding up and streamlining the process.

Second, there is a risk that the Phase II reference rate may increase unnecessarily. A particular strength of the OFT's merger work was its flexibility and substantive focus while being relatively "process-lite". It would be unfortunate – both for merging parties and the taxpayer – if the CMA lost some of this flexibility, so that there was an unnecessary increase in the number of cases referred to Phase II – ie cases that were referred and subsequently cleared – particularly if there is no scope for appropriate cases to be closed down quickly at Phase II.

Third, some of the changes – in particular, the enhanced hold-separate powers at Phase I – risk undermining the voluntary nature of the regime and its benefits for M&A activity if, for example, they have the effect of increasing the number of non-problematic cases that are notified to the CMA.

Finally, none of the changes appear, at least directly, to address the government's concern about some anticompetitive mergers escaping review.

Much will, of course, turn on the CMA's application of its new powers in practice. Mindful of the effective operation of the old regime, it is hoped that the CMA will exercise caution. There is a risk otherwise that the strengths of the voluntary regime are undermined, so that merging parties might actually prefer the certainty of a mandatory filing regime, as exists elsewhere in Europe and around the globe – something that the government clearly decided against.