Do competition watchdogs need clearer vision or sharper teeth, when combating cartels?

ALSO IN THIS ISSUE
- Gains drive consumer switching
- Centre for Competition Policy Annual Conference focuses on institutions
- What is the price of pay-to-delay deals?
- Behavioural Economics in Competition and Consumer Policy
- How a European Commission press release has potentially caused significant changes to the use of injunctions in the context of standard-essential patents
- What’s so wrong with retail price MFNs?
- UK public interest mergers: uncertain times ahead
Do competition watchdogs need clearer vision or sharper teeth, when combating cartels?

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Can an antitrust watchdog economise on the cost of enforcement by increasing corporate fines? Recent CCP research on the effectiveness of investigation and fines suggests that they might be able to do so.

As cartels continue to exist and numerous companies still engage in price fixing, market sharing and the like, antitrust enforcement appears to struggle to protect competition. A common critique, which has recently been brought to the attention of the general public by The Economist, is that fine levels need to be higher to deter corporate crime. Well aware of this issue, antitrust authorities in different countries have begun to sharpen their teeth. For example, the fining policy of the UK’s Office of Fair Trading (OFT) became substantially tougher last year. Whereas previously a collusive behaviour was punishable with a fine of up to 10% of the relevant worldwide turnover, the OFT has recently increased this figure to up to 30% of the relevant worldwide turnover. But, since there are costs associated with higher fines, such as possible bankruptcy, which may ultimately harm consumers, should the watchdog instead have clearer vision, i.e. be more alert and increase their investigative efforts?

Antitrust authorities in different countries have begun to sharpen their teeth.

Since Gary Becker's influential paper on the economics of crime in 1968, economists have postulated that firms base their decision of whether or not to cartelise a given market on a comparison of the expected costs and benefits of this unlawful action. A firm will opt to engage in criminal misconduct when the economic gains from participating exceed the expected costs of the illegal activity. As the economic gain, in general, lies outside the direct control of antitrust legislation, policy makers are left with two ways to increase the expected cost: they can either increase the likelihood of detection and prosecution, or they can increase the severity of the punishment imposed. Of course, the probability of catching an offender is related to the capacity of the antitrust agency, and hiring skilled staff is costly. Hence, mainstream economics suggests that enforcement agencies should economise on the cost of enforcement by committing fewer resources to detection, while achieving the same deterrence effect through an offsetting increase in the fines levied upon offenders. For authorities facing tough budget restrictions (the OFT faces a 5% year-on-year budget reduction), this policy recommendation is very attractive. Recent research by CCP tries to guide both legal and economic discussions on whether combining tougher fines with reduced investigation effort is indeed a valid option.

The problem with providing academic advice, however, is that it is quantitatively difficult to isolate the degree of deterrence provided by a single enforcement component. Additionally, we cannot empirically measure the individual actions of all the cartels that may have (or have not) been deterred by given policy changes. Luckily, these problems...
do not exist in the laboratory, where market conditions can be simulated and economic experiments can be run. For nearly half a century economists (including Nobel laureates Reinhard Selten, Vernon Smith and Al Roth to name a few) have used experiments where human subjects play the role of economic agents and are paid according to their performance. Experimental methodology allows one to observe the effect of a policy induced change in key parameters in ways that are not possible outside the controlled environment of the laboratory. Applications of this method can be found in the recent book, ‘Experiments and Competition Policies’.

We utilise this cutting-edge methodology to examine how the magnitude of the fine levied on a firm and the likelihood of antitrust punishment affect the choice to participate in a (illegal) cartel. In this experimental world, each subject plays the role of a firm, competing in a market involving price competition. The firm charging the lowest price captures the whole market. This market process is then repeated multiple times. Firms can form a non-binding price cartel; however such collusion is deemed illegal and, if detected, can result in financial penalties. We consider two initial cases: in one case the likelihood of getting caught is low, but the fine level is high; whereas in the other case the detection rate is high and the fine level is low. The expected cost to firms (detection rate multiplied by fine amount) remains identical in the two cases, allowing us to compare the relative effectiveness of a high fine and low detection regime, as opposed to a low fine and high detection policy. Additionally in two further cases, similar to the ones described above, we allow subjects to self-report the existence of a price fixing cartel in return for a reduction in fines. This makes it possible to explore the robustness of our findings in the presence of a leniency policy.

Based on the data obtained from the experiment, we find that, when leniency is not available, fine magnitude and likelihood of punishment seem to be interchangeable instruments to deter cartels. Comparing the percentage of firms (participants) in favour of cartel formation, we observe no statistically significant difference between those firms (participants) that faced a high fine with a low detection probability and those firms (participants) that faced low fines with a high likelihood of detection.

As can be seen from the chart, a leniency policy works well. In both the high fine low detection scenario and the low fine high detection scenario, the percentage of cartelised markets is lower when a leniency policy exists. However, when leniency exists, for the high fine low detection case the percentage of cartelised markets is significantly lower than for the low fine high detection case, a difference which is not shown when leniency is not present. This brings good news for a watchdog, such as the OFT, who implements a high fine regime under a leniency program. Furthermore, we investigate whether a tougher punishment leads to cartels raising their prices by a larger amount. If firms react to higher fines by increasing their overcharge, welfare concerns might make it undesirable for authorities to increase their corporate fines. Bringing further good news for the OFT, we find no support for this potential response by firms.

Why does the policy indifference between the high fine low detection scenario and high detection low fine scenario hold in the absence of leniency, but not when a leniency policy exists? A possible answer is that, due to self-reporting, firms (participants) may assume a different likelihood of detection when a leniency program exists. The likelihood that another firm self-reports may well depend on the fine levels, as higher (lower) fines provide a stronger (weaker) incentive to self-report, all else being equal.

So, in summary, do competition watchdogs need sharper teeth (with or without clearer vision)? As far as our experimental results suggest, they do.


Gains drive consumer switching

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The energy regulator has tried to increase fairness by preventing companies from offering cheaper prices to consumers who they attract from other suppliers compared to the prices charged to their existing customers in their home region. This policy resulted in a fall in potential savings, and a halving of switching rates, which in turn has caused concern and led to further regulatory policy intervention in the Retail Market Review.

Consumer activity plays a crucial role in securing effective markets because the way in which consumers search, and eventually switch, provider can have a substantial impact on market power and competition. Three strands of research at CCP underline the importance of potential monetary gains in increasing consumer activity in the energy market. The first links information people in charge of choosing the energy supplier for their household tell us about their searching and switching activity with their expectations of monetary gain; the second analyses data from a collective switching exercise in Spring 2012; and the third relates the aggregate numbers switching supplier to the potential gains available in the market across regions over the past eight years. The methodologies have different strengths and weaknesses, but all come to the same conclusion, namely that the major driver of consumer activity is the gain available.

Two major surveys of individuals in Great Britain who were responsible for choosing the energy suppliers for their households were conducted in 2005 and 2011. These surveys asked the respondents how much they expected to save by switching and whether they had looked around for a better deal and/or switched to a better deal. These surveys build on an earlier study of switching behaviour looking at the period when the British gas market was first opened, which identified the importance of potential gains in motivating switching. The 2005 survey asked about eight different markets (electricity, telecoms and broadband and financial services), and the 2011 survey focused on electricity. In both cases, econometric analysis showed that, after controlling for other factors, those who thought they would make greater savings were much more likely to be active in the relevant market. This result applies not just to an average or representative consumer, but also to households who report rather different characteristics.

One innovation in the analysis of both surveys is that additional detail concerning consumers’ characteristics was included, allowing for variation in experience and attitudes to be considered. This analysis showed that the effect of gain was stronger for some groups than for others. For example, in the 2011 survey, we found that those who are actively looking for better deals in the market are no more likely to search when their expected gains are high, because they are already actively engaged in search; but among this group, as among all the others, those who expect higher gains are more likely to switch suppliers. So whatever the attitudes of the respondents to markets, they were more likely to be active when their expected potential gains were higher. The 2005 survey showed that, because of differences between consumers’ attitudes to gains, to achieve high switching rates expected gains had to be very large. For example, to achieve a switching rate of 80% expected gains as high as £100 per month, around twice the average bill, were required.

These studies had the advantage of asking consumers how much they had expected to gain from engaging in the market, their characteristics and their attitudes; however, they had the drawback of depending on respondents’ ability to recall both their actions and their expectations. Moreover, some of the least active participants could not give us estimates for their expected savings from switching supplier. As such, the sample we could analyse was unrepresentatively ‘active’ compared to the population as a whole.

A similar selection bias applied to our analysis of participants in a collective switching auction, where those joining had opted in to the exercise and, therefore, represented an exceptionally active group of households. However, in this study we were able to observe both the actions which the participants took (to switch or not to switch) and the actual offer which they had received to motivate this (in)action, as well as many other characteristics of their energy demand. Again, we found that among this group, after controlling for...
other factors, potential gains were the main driver of whether or not a consumer switched supplier.

In another study we were able to analyse the total number of consumers recorded as switching in each of the fourteen electricity regions in Great Britain for each month from 2005 to the present. These aggregate switching figures were then related to price differences in the market. Even though we were unable to disaggregate these switches according to the companies from whom, and to whom, the switch occurred (due to reasons of confidentiality) the analysis confirmed that the main driver of switching was price differences. The change in potential gains over time and the base line costs of energy bills also contributed to switching rates. This confirms both ‘push’ factors (when energy prices rise, they become more salient to householders and so householders are more likely to switch) and ‘pull’ factors (consumers are more likely to switch supplier when there are larger potential savings).

That consumers are more likely to switch if (they believe) the gains from switching are higher may seem to be stating the “bleedin’ obvious”, but these findings hold important reminders for policy makers. From the government, Nick Clegg and David Cameron have called for the automatic placing of all householders on the cheapest available tariff, and the leader of the opposition, Ed Miliband, has promised to freeze energy prices if elected. All of these remedies, proposed for understandable reasons, are likely to reduce the gains available from switching and, on the basis of the evidence reported here, to reduce switching activity still further. As the Retail Market Review proposals are implemented, we already see the withdrawal of cheaper offers, as companies are restricted in the number of tariffs they are allowed to offer. These policies may be justifiable on grounds of fairness or holding down living costs or political expediency, but they will dampen consumer activity – why should consumers switch if there is little to gain?

Why should consumers switch if there is little to gain?

Consumers are crucial players in providing companies with an incentive to offer good deals and keep costs and prices down. If prices are constrained, so consumers have little to gain by switching between energy providers, then the energy providers are unlikely to provide a good deal for the very consumers which the present policy interventions are designed to protect. The danger is that current policies will suppress residential energy price differences, the engine of consumer activity, without introducing adequate alternative sources of discipline on the companies who provide this vital commodity.

3: Paper in draft form, available from the authors on request.
4: Paper in draft form, available from the authors on request.
The 9th CCP Annual Summer Conference was held in June 2013 and focused on institutions and competition policy. The event included presentations across CCP’s areas of expertise and raised important questions about the history and effectiveness of institutions related to competition. Other important questions raised concerned the role of international networks, different methods of enforcement, emerging economies and ongoing reforms across Europe. Contributions from a diverse and international group of academics and practitioners were complemented by a keynote speech by Bill Kovacic.

The conference opened with a keynote speech by Bill Kovacic (George Washington), who discussed how to achieve a better understanding of institutional design, better incentive systems and improved performance management regarding competition agencies.

In a session dedicated to the history of institutions, Laurent Warlouzet (Artois/LSE) drew on his personal research of the EU archives to provide historical overviews of EU institutions and how EU competition policy developed alongside the single market. Stephen Martin (Purdue) compared the changing views of the first and second Chicago School economists (i.e. Simons and Director) with subsequent generations (from Bork and Posner to Priest and Stigler) in light of their potential influence on US courts.

Economic viewpoints on the effectiveness of institutions were introduced by Tomaso Duso (DIW Berlin), who asked whether competition policy is socially beneficial, before presenting research into mergers to answer the questions of how to measure competition policy and its effectiveness. This session was complemented by joint research by CCP’s own Bruce Lyons, Prishnee Armoogum, Steve Davies and Peter Ormosi. Bruce Lyons reviewed methods of assessing the performance of competition agencies. He used Global Competition Review ratings to establish that factors determining the reputation of agencies include scale, national governability and type of legal system, before concluding that investment in well-qualified economists could be more beneficial than having a high proportion of lawyers within an agency. Steve Davies assessed the level of potential anti-competitive harm in an economy, and the degree to which competition agencies can successfully prevent such harm. He highlighted the endemic selection bias in the evaluation of competition policy. This occurs due to the lack of empirical observations regarding deterred and undetected cartel cases. In the case of undetected cartels these unobserved cases are likely to be the most harmful. However, the unobserved cases of deterred anticompetitive mergers are likely to have a positive impact on the selection bias.

The day ended with a session devoted to networks, with Imelda Maher (UCD) presenting research into the transparency and accountability of networks of competition agencies, and Hussein Kassim (CCP) and Kathryn Wright (York) introducing their joint work on the European Competition Network, ten years after modernisation. Discussions and networking continued over dinner at The Assembly House in Norwich, and over drinks at one of the city’s historic pubs.

The conference resumed on the second day with a session on institutional reform focussing on competition agencies across Europe, with the Netherlands serving as a point of
reference.

In Spain, competition law and regulation enforcement have been integrated with the merger of the national competition authority and six regulators into a single agency. Francisco Marcos (IE Madrid) explained that this was motivated by a need to increase efficiency, generate savings and improve independence. The new National Commission of Markets and Competition (CNMC) is intended not only to preserve and promote effective competition, but also to carry out specific control of a variety of sectors (from electronic communications to transport). These objectives are set against a backdrop of budgetary and personnel constraints and intervention by the European Commission.

Maarten Pieter Schinkel (UVA) joined us via Skype from Amsterdam to present his overview of the new Dutch Authority for Consumers and Markets (ACM). This authority was created on 1 April 2013 following a speedy two year merger process combining the former Dutch Competition Authority, the independent postal and telecoms authority and the consumer authority. He highlighted concerns about significant ministerial influence over the agency (from appointing the Board and approving ACM policy rules to annulling ACM decisions) and concluded that there had been a missed opportunity for smart institutional design.

For France, Thibaud Vergé (CREST) provided an overview and evaluation of reforms, whereby the Autorité de la Concurrence assumed duties as a single agency for competition and merger control in 2009 (replacing the dual approach of the Council for Competition and the Ministry for the Economy). He outlined the effects of the reforms, which had both positive outcomes (e.g. greater independence to carry out inspections and a less politicised merger process) and negative results (e.g. loss of interaction between local and national investigators and fewer cases being referred by the ministry).

Alex Chisholm (Chief Executive Designate, UK Competition and Markets Authority (CMA)) introduced the new CMA which will see the Office of Fair Trading (OFT) and Competition Commission (CC) evolve into a single agency. In contrast to other countries, where the merger of competition authority and regulators is a response to financial and policy constraints, the CMA appears unlikely to represent a radical departure from the current policy practice of the OFT and CC. Indeed, the need to maintain the “marriage” of consumer and competition work is acknowledged, recognising the experience of other countries. The CMA’s aim is to defend consumer interests by promoting competition, increasing and improving enforcement, increasing the transparency and speed of the competition regime and by ensuring that working practices are more flexible and productive.

The penultimate session looked at enforcement, in particular, the role of the specialist tribunal and the relative merits of inquisitorial and prosecutorial models. Peter Freeman (Chairman, UK Competition Appeal Tribunal) considered alternative decision-making models and reviewed the role of the courts in private actions and in appeals against competition authority decisions. He strongly favoured a specialist tribunal, but warned that tribunal independence may be compromised, if government views the agency as simply another part of the competition system rather than as a court upholding the law. Jacques Steenbergen (Director-General, Belgian Competition Authority) identified factors determining the relative merits of inquisitorial and prosecutorial systems as being independence and efficiency. He concluded that there is no “one-size-fits-all” model. The prosecutorial model is dependent upon the availability of an appropriate court or tribunal, while the inquisitorial model benefits from a separation between investigative and decision-making powers and dual models suffering from being more resource intensive.

The conference closed with an insightful consideration of institutions and emerging economies. Hassan Qaqaya (Head of the Competition Law and Consumer Policies Branch, UNCTAD) considered the problems and effectiveness of competition policy in emerging economies, specifically, the interplay between competition policy and other social or public policies. Competition agencies do not operate in a vacuum, and need to consider the views of consumers and the business community as well as regulators and policy makers. Finally, Sean Ennis (Senior Economist, OECD) outlined the economic challenges faced by emerging economies (e.g. high levels of poverty, highly concentrated ownership patterns, poor regulation of monopolies and unreliable government funding of agencies) and how this can impact the prioritisation of competition law and policy. Several of the speakers at this year’s conference were interviewed about the main points from their presentations. You can see the video of these interviews at: http://competitionpolicy.ac.uk/summer-conference-2013

This brought a very interesting and thought-provoking conference to an end. Already, we are looking forward to welcoming you next year to our 10th CCP Annual Summer Conference which will be held on 12-13 June 2014. The focus will be on ‘problem markets’ which sometimes seem to be ‘too hot’ to handle. Further information can be found on our website.
What is the price of pay-to-delay deals?

Farasat A.S. Bokhari, Senior Lecturer in Economics

When a branded drug manufacturer makes a payment to a potential entrant to delay entry of a generic drug, it raises anticompetitive concerns. In this report, I highlight one such deal in the market for drugs used to treat attention deficit hyperactivity disorder (ADHD)—mixed amphetamine salts (MAS)—and compute market equilibrium prices under three counterfactuals. In the first case, equilibrium prices are computed as if all MAS drugs were produced by a single profit-maximising firm. In the latter two counterfactuals, I compute equilibrium prices as if either an immediate-release (IR) generic or an extended-release (XR) branded drug were not available in the market. The simulations show that the average percentage increase in drug prices is 4 to 4.5 times larger in the latter two cases (when one of the drugs is not available in the market) compared with simple joint profit maximisation when all the products are available. In this respect, the challenges by the Federal Trade Commission (FTC) to so-called “pay-to-delay” deals and the recent legislation introduced in the US Congress to ban such deals are justified.

In August 2006, Shire PLC and Barr Laboratories reached an agreement—a pay-to-delay deal—where, in return for a net payment from Shire arising from other side deals between the two manufacturers, Barr Laboratories would not market a generic version of Shire’s blockbuster drug Adderall XR in the US until April 2009, at which point Barr would enter as a generic maker under licence from Shire. A pay-to-delay deal involves a payment from a branded drug manufacturer to a generic maker to delay market entry. This report considers these entry limiting agreements in one pharmaceutical segment—psychostimulant drugs used for the treatment of attention deficit hyperactivity disorder (ADHD)—and computes simulated market equilibrium prices to gauge the impact of the pay-to-delay deals.

Under the terms of a typical pay-to-delay deal, a pharmaceutical company holding a patent on a drug enters into an agreement with a generic challenger where, in return for withdrawing the challenge, the generic firm receives a payment and/or authorised licenced entry at a later date, but before the expiration of the patent itself. Pay-to-delay deals are increasing on both sides of the Atlantic. In the US, while there were 3 agreements involving a restriction on generic entry and a payment to the generic maker in 2005, there were 19 such agreements in 2009 and 31 in 2010. Similarly, in 2010-2011 in the EU/EEA zone, there were 13 settlements limiting generic entry which involved a payment (“value transfer”) from a branded drug company to a generic drug maker.

Due to antitrust concerns, the US Federal Trade Commission (FTC) has challenged these settlements as a top priority and sued several pharmaceutical firms in different district courts. Until recently, the courts generally upheld these settlements under the ‘scope of the patent test’ since the delayed generic entry still took place prior to the expiration of the patent. However, in a recent decision by the Third Circuit Appellate Court of the US, regarding a pay-to-delay deal between Schering-Plough and the generic maker Upsher-Smith over K-DUR 20 (an XR form of potassium chloride used to treat high blood pressure) the court found “prima facie evidence of an unreasonable restraint of trade”. The court expressed the view that the scope of the patent test restricts the application of antitrust law and is contrary to precedent on patent litigation and competition. This decision was in contrast to an earlier decision by the Eleventh Circuit, and the K-DUR 20 pay-to-delay case is now before the US Supreme Court.

On this side of the Atlantic, the European Commission is also investigating similar deals and has issued a ‘Statement of Objection’ in three cases in recent months.

The case of delayed entry by a generic version of Adderall XR, as analysed in this paper, is similar in many respects to
In 1999, Shire’s Adderall had a 21.6% share of the market for all ADHD drugs. The generic version of Adderall (i.e. MAS-IR generic) entered in 2002 and by the end of 2003 there were three generic makers of this formulation. However, in order to protect its market share, in 2001, Shire introduced a 12-hour (XR) version of Adderall - Adderall XR. By 2003, Adderall XR was a blockbuster drug with nearly 25% of the market for all ADHD drugs in the US. At this point, Barr Laboratories and Impax Laboratories filed Abbreviated New Drug Applications (ANDAs) with the Food and Drug Administration to market generic versions of Adderall XR. Under the terms of the Hatch-Waxman Act, Shire had a market exclusivity period until April 2005, but two key patents on the XR formulation further prevented entry in the MAS-XR segment until 2018. Consequently, Shire sued Barr and Impax for patent infringement with the case between Shire and Barr being scheduled for trial in January 2006.

Shire settled with Impax (the second ANDA filer) in January 2006 and allowed it to market the generic version of Adderall XR under its own licence prior to January 2010. Since Impax was the second filer of the ANDA application, and not entitled to six month exclusivity under paragraph IV of the Hatch-Waxman Act, Shire did not offer an exclusive licence to Impax. Following this deal, in August 2006, Shire and Barr also reached a settlement where Shire agreed to grant Barr Laboratories a 180-day exclusive licence to market generic Adderall XR in exchange for delaying entry until April 2009. True to the terms of the deal, Teva Pharmaceuticals (which now owns Barr Laboratories) introduced generic Adderall XR on April 2, 2009 and Impax started shipping its generic version on October 2, 2009. According to the press release by Shire, no payments were made by Shire as part of the settlement of the Adderall XR dispute. Nonetheless, there were a series of complex side deals between the parties involving value transfers and product acquisitions with a net payment of $102 million from Shire to Barr.

Using previously estimated demand system parameters, this paper simulates equilibrium prices of all ADHD drugs under three scenarios and compares them to a baseline of observed US prices in 2003. In the first scenario, prices are predicted when Shire and the generic makers of MAS-IR (i.e. Shire’s 4-hour MAS tablet) set prices so as to maximise their joint profits. The idea is that if generic MAS-IR had entered under a licence from Shire (i.e. an authorized generic entry, as sometimes occurs under delayed entry deals) prices would be mutually agreed upon to maximise the firms’ joint profits. In the second and third scenarios, out of sample projections are used to simulate the cases when either generic Adderall is not available in the market, or Shire’s branded Adderall XR is not available in the market. The latter two scenarios are relevant because, although generic Adderall XR entry did not take place until much later, this drug shares characteristics just involving the same molecule and form but more widely, such that the prices of all the other drugs, and not just MAS drugs, increase quite significantly. The average price increase, or equivalently the increase in average profit margin (assuming costs do not change), is 4.1-4.5%.

In all three counterfactuals, there is a significant increase in the price of ADHD drugs, however, the percentage increase is 4-4.5 times larger in the case of a missing drug compared to when the prices of Adderall and its generic versions are set jointly to maximise profits. In a typical pay-to-delay deal, both features may be present: a 2-3 year delay in any generic entry (whether authorised or independent) followed by a term of licenced entry and joint profit maximisation. In this respect, the challenges by the FTC to the ‘pay-to-delay’ deals, recent legislation introduced into the US Congress to ban such deals, and the investigations by the EU Commission are justified.

1: This paper is based on Bokhari, F. (2013), ‘What is the price of pay-to-delay deals?’, Journal of Competition Law and Economics, 9(3), 739-753.
Recent years have seen academics and policymakers take a keen interest in the implications of behavioural economics for competition and consumer policy. *Behavioural Economics in Competition and Consumer Policy* has been written by CCP researchers from economics, law, politics and business management; it reflects their interest and expertise in the area and the Centre’s multidisciplinary approach to policymaking. The book draws on the insights researchers have acquired - through surveys, experiments, theoretical work and market case studies - into specific behavioural issues and how these may or may not be resolved by intervention. It is aimed at policymakers and practitioners who may be weighing up whether, and how, to take the evidence on behavioural traits into account when considering intervention in markets. The book has been written in a way which we hope will make it accessible to a wide range of readers, whether in public, private or third sector organisations. It can be read as an introduction to the area, or as a reminder and a reference point to the more detailed analytical studies that are available. This article provides an outline of the book, pointing to the key themes and issues appearing in each chapter.

Following an Introduction and a Glossary, *Behavioural Economics in Competition and Consumer Policy* is divided into three parts, with each part including real-world case studies.

**Part 1 provides an introduction to the terrain of behavioural economics and its implications for competition and consumer policy**

In *Chapter 1: Consumer Behaviour and Market Competition*, Enrique Fatas and Bruce Lyons discuss the ways in which consumer decision-making may not be fully rational and how firms can exploit such behaviour. In particular, the chapter points to how some people are unable to collect and process all the available information that would potentially help them make a rational decision; where this is the case, some firms will have an incentive to obscure key decision-relevant facts so that these behavioural consumers end up paying higher prices or buying lower quality products than if their decision-making skills were unbounded. The authors consider the remedies that are appropriate for interventions founded on behavioural economics. A major issue in this regard – and one that resurfaces in later chapters of the book – is how to design a remedy such that, in correcting one distortion of the market, the remedy doesn’t introduce a new one. Fatas and Lyons conclude that competition and consumer policy does have an important role in helping consumers obtain better market outcomes, but that it needs very careful design if it is to avoid doing more harm than good.

It is aimed at policymakers and practitioners.

In *Chapter 2: Making Sense of Complex Choice Situations*, Judith Mehta and Robert Sugden pick up on a key topic of the previous chapter: the price complexity that may be introduced by some firms and its impact on the market. The topic is addressed in the context of the information revolution and the explosion of internet commerce. Yes, more information is now available to us; and, sometimes for good but sometimes for ill, this has made it easier for firms to know more about their customers. The authors describe some of the pricing practices deployed
by firms - drip pricing, baiting, price partitioning and complex offers - and they discuss the impact of these on consumers and on the efficiency of the market. But they also discuss some of the market’s self-regulating tendencies which work against such anti-competitive and exploitative practices. The second major topic of this chapter is the concept of ‘choice overload’. The authors ask whether this describes a genuine phenomenon: is choice something that ‘no longer liberates, but debilitates’ to the point where we can say there is too much choice? The authors conclude that choice overload is a genuine phenomenon in certain types of choice environment, but they also warn against an overly extravagant rhetoric with the potential to lead to protectionism.

Then in Chapter 3: Social Influences on Behaviour, Shaun Hargreaves Heap draws on theory and evidence from experiments to discuss the ways in which people’s choices often seem to change as a result of social influences. These influences are various, as are their implications for policy. The author points to how the behaviour of others can transmit useful information to observers about how best to satisfy their preferences, but also how it can lead to networks of people becoming locked in to suboptimal outcomes. The author also observes that people’s preferences are not always as well-formed as standard theory presupposes; under these conditions, preferences can be influenced by those of the people one associates with, which is why many individuals are drawn to follow what others do. These and other situations in which people are influenced by those around them point to the scope for new kinds of policy, to new issues in the conduct of competition and consumer policy and, ultimately, to questions concerning whether efficiency can be the criterion for guiding policy.

Part 2 of the book turns to empirical case studies. Chapters 4 and 5 focus on the belief that consumers play a vital role in the competitive process by being ready and willing to move their custom to where the best deals are available, thereby providing an incentive to firms to cut prices and improve quality. This being the case, issues arise for policymakers when some consumers appear to manifest inertia, that is, a reluctance to switch provider.

In Chapter 4: Searching and Switching Across Markets: Is Consumer ‘Inertia’ the Result of a Mistake or a Preference?, Minyan Zhu draws on responses to a CCP survey of consumers to address the question of why some consumers search and switch, some search but don’t switch, and others neither search nor switch. Having reviewed the evidence from several different markets, the author concludes that, in a number of cases, it is questionable whether the failure to switch is the result of biased decision-making or error, and suggests that it may be instead the result of a preference to stay with the current supplier.

Chapter 5: Shedding Light on Consumer Behaviour in Energy Markets focuses specifically on energy markets, a sector where policymakers have been disappointed by low levels of switching. Catherine Waddams Price presents evidence from surveys and experiments to shed light on why this might be the case and then considers the solutions that might be imposed. The author finds that intervention is not straightforward because different people react very differently to the market: some consumers are active and some are not, and firms have learnt to discriminate between the two, offering better deals to those who are active compared to those who are content to stay with their current provider. The author concludes that policy aimed at raising consumer activity needs to take account of these differences if it is to be effective, and not to introduce unintended adverse consequences.
Part 3 of the book both looks back and projects forward. We reflect on what has been learnt about the behavioural consumer in theory and through the experience of a number of behavioural remedies. We then consider where a new body of literature is taking us with respect to policymaking.

In Chapter 6: Behavioural Remedies in Final Consumer Markets: Theory and Evidence, Morten Hviid draws on a series of case studies and examples to examine the problems which can arise for consumers before, at and after the point-of-sale, and the remedies designed to address these problems. The author points to two key problems facing consumers in choosing between products (or, indeed, in determining whether or not to make a purchase at all): first, the problem of acquiring the information necessary to make a decision and, second, the problem of processing that information in order to make the best use of it. The author discusses the conditions under which the market may spontaneously address these problems before turning to situations in which intervention becomes necessary. Some of the difficulties associated with implementing remedies are discussed, as well as the conditions which must be in place for a remedy to be effective and for it not to deliver unforeseen consequences. In the face of the difficulties, the author stresses the importance of evaluating proposed remedies. Accordingly, this chapter includes a section in which Franco Mariuzzo discusses econometric approaches to the assessment of markets before and after the introduction of remedies and a novel technique designed to enhance our ability to assess behavioural remedies.

Chapter 7: Behavioural Remedies and Cost-Benefit Analysis: A Cautionary Note takes a close look at a particular niche within behavioural economics, the literature of ‘behavioural law and economics’ and the kind of remedies proposed under this heading by legal academicians. This literature draws on insights from behavioural economics to suggest that interventions can be devised to steer individuals towards choices which make them better off. For example, a mandatory cooling-off period may be introduced to ensure consumers have an opportunity to reflect on the product on offer and to check on the availability of competing products. Michael Harker and Judith Mehta point to a number of issues arising from this approach, including the potential for behavioural remedies to be challenged in the courts and the danger that unintended consequences will result from remedies. They also point to the difficulties associated with assessing the welfare effects of an intervention, difficulties that are exacerbated in a world in which some, but not all, consumers are characterised by bounded rationality and/or non-standard preferences.

In Chapter 8: Modelling Naïve Consumers: What Does Behavioural Economics Tell Us About Market Outcomes?, Amelia Fletcher discusses an emergent literature, one which takes the basic tenets and mathematical modelling approach of game theory but then combines this with alternative assumptions on decision-making in order to examine how the analysis is changed. The author identifies three strands in this literature: the first strand treats switching and search costs as the product of behavioural biases with firms able to influence these costs; the second introduces behavioural biases into models of asymmetric information; and the third focuses on behavioural biases that lead consumers to mis-estimate their own demand. The author points to important insights being generated by the new analysis, in particular, around the ways in which firms will tend to adapt their strategies to exploit consumers’ behavioural biases. In considering the implications for competition and consumer policy, one interesting result is that more competition will not necessarily solve the issues discussed and, indeed, increasing the level of competition can actually make things worse. In conclusion, the author observes that there is an easier fit between the emergent behavioural economics and consumer law and its enforcement than in an earlier era when the focus was on hyper-rational consumers. On these grounds, she anticipates a future in which greater use is made of behavioural economics in the design of competition and consumer policy.

Behavioural Economics in Competition and Consumer Policy is available now. If you would like a copy (either a print or electronic version) and you have not already contacted us, please send your details to: J.Mehta@uea.ac.uk
How a European Commission press release has potentially caused significant changes to the use of injunctions in the context of standard-essential patents

Sven Gallasch, Lecturer in Law

In March 2013, the District Court of Düsseldorf decided to refer a patent dispute concerning the use of injunctive relief in the context of standard-essential patents (SEPs) to the Court of Justice of the European Union. This decision is noteworthy for a number of reasons. Firstly, it is likely to harmonise the use of provisional remedies in relation to SEPs across Europe. Secondly, the issue is a hot topic and seems to be high up on the European Commission’s enforcement agenda. Thirdly, and most interestingly, the preliminary reference that is likely to resolve the issue was actually triggered by a European Commission press release. In the light of the on-going investigation by the Commission, the resolution of this issue by the Court of Justice prior to the potential final decision against Samsung is highly convenient.

Common standards are vital in any technology market. Without common standards we would all need to have a multitude of gadgets. In the 1980s we would have needed a Betamax player and a VHS player. Today, we would need a Blue-Ray player and one for HD-DVDs plus a number of different mobile phones - one for every available frequency which is used to transmit phone calls. Sticking with the mobile phone example, the reason why we only need a single mobile phone is called GSM, 3G and now LTE. These are the frequency transmission standards set by a standard-setting organisation (SSO) called the European Telecommunications Standards Institute (ETSI).

The resolution of this issue by the Court of Justice ... is highly convenient.

Every company that is a stakeholder in the IT & telecommunications sector is a member of ETSI and therefore takes part in the decision process which results in the setting of a relevant standard. However, these standards are generally covered by a patent, which is owned by one of the SSO members. This can lead, not only to a conflict of interest, but also allows the SSO member that owns the relevant patent to hold an entire industry to ransom. It could exclude any company that intends to use the set standard by means of patent infringement litigation or demanding extortionate royalties.

To avoid this undesirable situation, every SSO declares certain patents as ‘standard-essential’. According to the Rules of Procedure of ETSI, standard-essential means,
“that it is not possible on technical grounds, taking into account normal technical practice and the state of the art generally available at the time of standardization, to make, sell, lease, [...] use or operate equipment or methods which comply with a standard without infringing that [patent].”

Once a patent is declared as standard-essential, the owner of this standard-essential patent (SEP) is obliged to grant effective access to their patented technology to all market participants by means of irrevocable licences on fair, reasonable and non-discriminatory (FRAND) terms.

Not surprisingly, this kind of access is often contested and subject to patent litigation. The patent owner frequently seeks provisional remedies in the form of injunctive relief against the company that is already using the standard despite the patent dispute. This is the case in the patent dispute over the new LTE standard between Huawei Technologies and the ZTE Corporation which is litigated in front of the German District Court in Düsseldorf. In the lead-up to this litigation, the two parties negotiated the terms of the necessary licencing agreement for over a month without coming to a conclusion. During this time period, ZTE was already using Huawei’s patent, so Huawei sought injunctive relief against this use of its patent.

Under normal circumstances, the German court would have applied the so-called Orange-Book-Standard which is the legal test developed by the German Federal Court of Justice (BGH KZR 39/06) in 2009 to deal with the exact issue at hand – the question of under which narrow circumstances the owner of a SEP is allowed to seek injunctive relief against the alleged patent infringer.

However, the German court decided not to apply the Orange-Book-Standard in this case, instead referring the case to the Court of Justice (CoJ) by way of a preliminary reference. The German court explained that its decision to refer the case to the CoJ was literally triggered by remarks in a press release issued by the European Commission announcing the sending of a Statement of Objections to Samsung. Samsung was investigated by the European Commission for the seeking of injunctive relief against prospective licencees in the context of SEPs - a situation very similar to the dispute between Huawei Technologies and the ZTE Corporation in front of the German court.

How is it possible that a press release triggers a preliminary reference?

The paragraph of the press release that led to the referral to the CoJ reads as follows: “The Commission takes the preliminary view that the seeking of an injunction for SEPs can constitute an abuse of a dominant position in the exceptional circumstances of this case - where the holder of a SEP has given a commitment to license these patents on FRAND terms and where the company against which an injunction is sought is willing to negotiate a FRAND licence.”

According to the District Court in Düsseldorf, the approach hinted at by the European Commission, and especially the emphasis simply on the willingness to negotiate, is in stark contrast with the Orange-Book-Standard which it would have normally followed to decide the dispute between Huawei Technologies and the ZTE Corporation.

According to the Orange-Book-Standard judgment, the defendant (ZTE Corporation) could have only sought the so-called FRAND defence against the plaintiff’s (Huawei
Technology) motion for injunctive relief order, if a number of strict requirements were satisfied. With this defence, ZTE could have asserted that Huawei is abusing its dominant position by means of seeking injunctive relief against ZTE’s use of the patent in question, due to the fact that ZTE is a prospective licencree of a SEP on FRAND terms. In order to succeed with this defence, however, ZTE would have been required to show the following:

1. ZTE would have needed to offer Huawei an unconditional licencing agreement, which ZTE is bound by. The offer could not have been made under the condition that the court finds the patent to be infringed.
2. ZTE would have had to act as if the offered licence had already been accepted. In case the patent in question had been used before Huawei had accepted the offer, ZTE would have had to account for the use of the patent, calculate the royalties and make payment according to these calculations into an escrow account.

ZTE would not have been able to satisfy the Orange-Book-Standard criteria, as neither had it made an explicit offer nor had it made any payment in relation to a hypothetical licence agreement. Thus, a few months earlier, the District Court would have dismissed ZTE’s FRAND defence. Yet, because of the European Commission’s press release, the German court decided to place the fate of this issue in the hands of the CoJ.

Does the District Court of Düsseldorf actually welcome the opportunity to refer the case?

It seems that the German court welcomed the opportunity to refer this issue to the CoJ. Apart from referring a number of questions regarding the correct approach to the FRAND defence against injunctive relief, the court offered its own opinion on the issue, arguing partially for but also against certain requirements of the Orange-Book-Standard.

The courts argued that the mere willingness to negotiate by the infringer is not sufficient to find an abuse of a dominant position, despite the patent holder’s declaration in front of the SSO that it would licence the SEP to third parties. The opinion recognises the incentives of both parties involved in FRAND negotiations over a SEP and tries to strike the right balance. This argument is in line with the Orange-Book-Standard.

The single requirement of the infringer’s willingness to negotiate would lead to a de facto per se prohibition for the patent holder to seek injunctive relief against the infringer. If the infringer did not have to satisfy further requirements, the patent holder would not only have to accept the on-going infringement, but would likely be faced with an infringer who could almost dictate the terms of the licence agreement, as the patent holder lacks any remedy to stop the infringement. This would leave the patent holder with significantly reduced bargaining power during the negotiation of the FRAND terms.

As a result, the District Court of Düsseldorf calls for the additional requirement of a binding offer by the patent infringer for the licence agreement. This offer includes all the specific terms and conditions that are common in the relevant industry. Such a requirement would not be disproportionate on the patent infringer as the infringer (usually a company trading in the relevant market) should have knowledge of the common standards in licence agreements that are normally used in the relevant area. Also, this would underline the seriousness of the infringer seeking the FRAND defence.

However, the District court is also of the opinion that the infringer ought to be allowed to make a conditional offer with regard to the validity of the relevant SEP. This line of argument departs from the strict Orange-Book-Standard. If the infringer were unable to challenge the relevant SEP, or if the patent holder were entitled to terminate the licence in the case of a patent challenge, it would mean that the validity of SEPs, which every market participant has to use, potentially could never be reviewed. The only possibility for a competitor to challenge the validity of a patent would be to commence court proceedings on the patent’s validity before the competitor started using the patent itself. Such proceedings are time-consuming and therefore could create a hold-up.

What are the likely implications of this preliminary reference?

The decision of the CoJ remains to be seen. The decision is not only likely to change the law regarding the use of remedies in the context of SEPs in Germany but also across the EU. This is because the CoJ’s decision will harmonise the judicial approach to motions for an injunction in the SEP context across Europe – a situation which is currently not given. For example, the German Orange-Book-Standard was rejected by courts in other Member States. The involved parties fought over the very same patents and issues in The Hague District Court where the court handed down a dissenting view expressly rejecting the German Orange-Book-Standard. The CoJ judgment will bring an end to such divergence and, ultimately, increase legal certainty for all parties across standardised industries and, even more importantly, across EU Member States. Nonetheless, until the CoJ has made its decision, similar proceedings across Europe are likely to be stayed.

It is doubtful that the parties in the referred case anticipated these wide-ranging implications, but the District Court of Düsseldorf seems to welcome the opportunity to challenge the Orange-Book-Standard set by the German Federal Court of Justice in 2009. From the European Commission’s standpoint, the referral is very convenient. The CoJ’s judgment will resolve a contentious issue regarding the use of provisional remedies in the context of SEPs before the European Commission issues its final decision in the Samsung investigation or, indeed, in other investigations in this context.

2: Ibid. §6.1.
3: Huawei Technologies v ZTE Corporation, District Court Düsseldorf, Germany, 21 March 2013, case no. 4b O 104/12
5: European Commission, ‘Samsung – Enforcement of ETSI standards essential patents (SEPs)’, MEMO/12/1021.
6: Koninklijke Philips Electronics N.V. v. SK Kassetten GmbH &co. KG, Joint cases No. 316533/HA ZA 08-2522 and 316535/HA ZA 08-2524.
What’s so wrong with retail price MFNs?

Amelia Fletcher, Professor of Competition Policy
Morten Hviid, CCP Director and Professor of Law

Retail Price MFN clauses have been at the heart of a number of recent antitrust cases. So what are these clauses? And why do they cause such consternation?

A number of recent antitrust cases on both sides of the Atlantic have involved a hitherto rarely observed form of Most Favoured Nation, or MFN clause. Such clauses, sometimes known as Retail Price MFN clauses to distinguish them from the more standard wholesale price MFN clauses, have primarily arisen in the context of online retail platforms. In particular, they lay at the heart of the US and EU e-book cases, UK and German cases relating to online travel agents, and UK and German investigations into Amazon Marketplace.

The authorities are now close to reaching resolutions in these various cases, with the parties either agreeing, or being required, to remove Retail Price MFN clauses from their contracts. But what are these clauses, and why have they created such consternation amongst competition authorities?

What are Retail Price MFN clauses?

Perhaps surprisingly, from a consumer perspective, these clauses may look like a ‘best price promise’, whereby a retailer promises consumers that they won’t find cheaper prices anywhere else in the market. In the case of Retail Price MFN clauses, however, there is an extra element; the ‘best price promise’ is enforced via an agreement with a third party supplier. It is the supplier that sets the retail prices across all retailers, and a Retail Price MFN clause signed with a given retailer ensures that the supplier’s retail price is no higher for that retailer than it is for any other retailer. If the supplier has reciprocal arrangements with a number of retailers, then the combined effect of these clauses is to create a parity, whereby prices are identical across these retailers.

The result is reminiscent of a Resale Price Maintenance (RPM) agreement within which a supplier sets identical retail prices across all retail outlets. In a bricks and mortar context, suppliers and retailers have remained nervous of entering into RPM or RPM-like arrangements, even where the law on RPM has been loosened, as it has been in the US following the Leegin case.1 Given this, it is perhaps not surprising that these clauses have been primarily observed among online retail platforms. These platforms have seen themselves as intermediaries between suppliers and their end customers, rather than as retailers in their own right, and have therefore considered themselves as sitting outside the law on Resale Price Maintenance (RPM). Their reasoning has been that either they are merely agents acting on behalf of their suppliers, or they are themselves upstream of the suppliers, providing distribution services as an input. In either case the law on RPM would not apply.

Whether or not online platforms have a valid legal argument in respect of the applicability of RPM law, two things are clear. First, the Retail Price MFN clauses can only exist if there is at least some form of RPM, in terms of it being the supplier that sets retail prices; otherwise the supplier cannot contractually commit to ensuring that retail prices will be the same (or no lower) in other retailers. In this context, it is noteworthy that the UK Office of Fair Trading took its online travel agency case as an RPM case, rather than a case specifically about Retail Price MFNs, but well aware that the termination of the RPM would automatically also bring to an end the offending MFNs.

Second, and perhaps more surprisingly, there is a reasonable case to be made that it is the Retail Price MFN clauses, and not the purely vertical RPM, that create the real consumer harm in these cases.

Why do Retail Price MFN clauses raise antitrust concerns?

To understand this, it is important to remember that RPM itself is intrinsically a purely vertical arrangement; it involves nothing more than an upstream supplier setting a downstream retail price. There is nothing intrinsically within RPM which means that the supplier has to set the same price in each retailer, and indeed we might well expect to observe a profit-maximising supplier setting different prices across retailers if these retailers were to charge the supplier different fee rates for their retail services.

This is an important point, but it is one that has hitherto not been recognised in the academic economic literature on RPM which simply assumes that each supplier sets the same prices across retailers. Effectively, RPM as analysed in the existing literature combines two elements: the intrinsic purely vertical element, whereby the supplier sets retail prices but under...
There is nothing intrinsically within RPM which means that the supplier has to set the same price in each retailer.

which prices can potentially differ across retailers, and an additional horizontal element which then acts to eliminate any such price differences.

However, it is interesting to consider the implications of these two elements separately. Where we observe only the purely vertical element of RPM, we find that the ability of the supplier to set differing prices across retailers can act as a crucial indirect competitive constraint on the fee rate charged by retailers to the supplier for using their retail services. How does it do this? If a retailer expects an increase in its fee rate to be passed on by the supplier in the form of a higher retail price at that retailer, relative to other retailers, then the retailer will typically expect to lose sales to competing retailers as a result. This threat of lost sales, in turn, will act as a competitive constraint on the retailer when setting its fee rates, and will act to keep these rates down.

This competitive constraint is important but fragile, in that it can be easily diluted, or even eliminated, though the use of Retail Price MFNs. Such MFNs effectively act in the same way as the horizontal element that is usually assumed to be part of RPM. With such an MFN clause in place, the retailer can raise its fee rate to the supplier knowing that there is no risk of the supplier setting retail prices higher for that retailer than for its competitors. For the supplier to do so, would be in breach of the Retail Price MFN. In turn, this means the retailer will expect to lose far fewer sales as a result of a fee rate increase, and this greatly reduces (or even eliminates) the indirect competitive constraint on the retailer’s fee rates. As a result, we would expect Retail Price MFN clauses to lead to higher retailer fee rates, and consequently higher retail prices.

A natural question to ask is why suppliers would ever sign up to such contracts, since retailers seem to get the upside in terms of higher retailer fee rates. It is noteworthy that the clauses were imposed by retail platforms, not suppliers, in each of the antitrust cases mentioned above. In practice, however, it is not clear that suppliers are made worse off, and they could potentially share some of the gains. Moreover, in an online arena, retail platforms can have a strong negotiating position relative to suppliers, since they deliver much-needed customers. As such, they may be in a good position to insist on Retail Price MFN clauses, even where these are not in the interest of suppliers. Moreover, Retail Price MFNs may help to keep the strong position of the incumbent platforms intact. Such clauses remove the potential for smaller firms to try to gain scale by offering lower retail prices than the incumbent in order to overcome the latter’s natural advantage.

Policy implications

What does this all mean in terms of the correct legal approach when assessing Retail Price MFNs? Recall that RPM effectively comprises two elements. The first, the purely vertical element, is relatively unproblematic from a competition perspective and indeed there can be efficiency benefits associated with this element. The second, the horizontal element, is the real driver of harm in the vast majority of RPM cases, but this has effectively the same impact as Retail Price MFNs. Moreover, while such MFNs can also give rise to efficiency benefits, these benefits are broadly the same as those that can arise from the horizontal element of RPM.

Retail Price MFN clauses are effectively the same as RPM with the good stuff taken out.

All of this suggests that Retail Price MFN clauses are effectively the same as RPM with the good stuff (i.e. the purely vertical element) taken out. As such, what does this mean for policy? It would seem reasonable to conclude that Retail Price MFNs are no less likely than RPM to have anti-competitive effects and no more likely to have efficiency benefits. Where to draw the line between presumed legality and presumed illegality of RPM has been the subject of much debate. However, on the basis of the above analysis, we suggest that, wherever the line is drawn for RPM, Retail Price MFNs should be treated equally harshly.

This article is based on Fletcher, A and M Hviid, “Retail Price MFN Clauses: RPM with the good stuff taken out?”, Antitrust Law Journal, forthcoming.

The recent competition reforms have intentionally overlooked the uncertainties that still engulf ‘public interest mergers’ in the UK. The Secretary of State retains a residual power to propose new public interest exceptions and there is speculation of what form these new interests could take. This note alludes to some of the proposals for new public interest criteria and considers the implications of these on the future of UK merger control.

As the dust begins to settle on the most expansive competition reforms in over a decade, one area that remains untouched by the UK Government’s reforms is its policy on the public interest and mergers. In many respects, it is unsurprising that the Government has sought to keep this issue off the agenda;¹ the controversy of public interest provisions could have overshadowed a number of other key proposals implemented under the Enterprise and Regulatory Reform Act 2013 (ERRA13). However, the reforms do mark another missed opportunity for the Government to address inherent uncertainties within the public interest provisions.

Once it becomes fully operational in April 2014, the Competition and Markets Authority (CMA) will assume the two-stage merger assessment procedure that is currently undertaken by the Office of Fair Trading and the Competition Commission. During a Phase 1 investigation, the CMA Board will assess whether a merger has resulted, or is likely to result, in a ‘substantial lessening of competition’ (SLC) within the relevant market. Where a transaction is found to raise these competition concerns, the Board, subject to proposing remedies, is under a duty to refer the merger to the CMA Panel for a Phase 2 assessment.² However, a departure from this default procedure is possible if the merger in question raises specific public interest concerns. Under the Enterprise Act 2002 (EA02), the relevant Secretary of State may intervene in cases raising national security and media plurality concerns;³ concerns which he or she may consider when deciding whether to refer the transaction to a Phase 2 assessment.⁴ In addition to these named interests, the Secretary of State also possesses a residual power to propose new public interest considerations by virtue of section 58(3) EA02. This residual power has particular significance as it allows the Secretary of State, subject to Parliamentary approval, to add to the specified public interest criteria without the need for statutory reform. As such, the recent competition reforms have had no effect on the potential for new public interest exceptions to be introduced in the foreseeable future. Although, of course, what has potential in theory and what is likely in practice are rarely consistent where ministerial discretion is present.

It is extremely difficult to predict the types of public interest that might be proposed by the Secretary of State under section 58(3). When the clause was first proposed as part of the Enterprise Bill, it was suggested that the Labour Government had only intended the Secretary of State to exercise the power in unpredicted and extreme circumstances.⁵ Indeed, these circumstances were so difficult to predict that Members from both Houses struggled to conceive of a situation where section 58(3) would be utilised. The answer finally arrived in 2008 when the Government forced through the Lloyds/HBOS merger using the public interest argument that it would ensure the stability of the UK financial system. But far from ushering in a string of new public interest criteria, this case has – to date – marked the only occasion where a Secretary of State has exercised the power to propose a new public interest criterion.

Further public interest factors have been suggested for consideration in future UK merger assessments, although, not one has yet come to fruition under the EA02. For example, Baroness Turner had proposed amending the Enterprise Bill to include employment as a named interest,⁶ an idea that was again discussed, alongside food security, in the aftermath of the Cadbury/Kraft merger.⁷ Also, others have anticipated mergers that raise concerns over the security of energy supply will materialise within the coming decade,⁸ a concern that is already given consideration in other merger regimes. For example, in South Africa both the Competition Commission and the Competition Tribunal have deviated from the competition-based approach to impose conditions on a merger to guarantee the provision of magnetite iron ore – a key

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component in the beneficiation of coal – to domestic firms.9

More recently, the Coalition Government has rejected a recommendation from Lord Heseltine to show a greater readiness to use public interest powers to combat foreign takeovers that threaten vital national interests in core sectors.10 The proposal attracted criticism for its ‘protectionist’ undertones, a characteristic which appears to fall outside the scope of the criteria intended to be applied under section 58(3). However, the prospect of industrial policy arguments was afforded weight by Lord Sainsbury in the House of Lords debate on the Enterprise Bill. In theorising about the application of section 58(3), he suggested the provision could be used to retain the domestic ownership of a new technology that is essential to the economic security of the UK.11 Lord Heseltine’s proposals perhaps go beyond the limited confines envisaged by Lord Sainsbury, but with certain large economies now adopting an openly protectionist approach to foreign takeovers,12 it is unsurprising that some commentators have called on the UK to follow suit.

Each of the interests referred to above is etched into the public consciousness. However, it is clear that it would take a very specific type of merger for any one of these interests to meet the extreme circumstances required under section 58(3). The fact that the Secretary of State’s power to propose new public interests is limited in this way offers respite to competition purists, who feel public interest criteria contaminate the long-term goals that competition strives to achieve. But it is unclear whether this power will continue to be applied in a restricted way. A lack of formal guidance leaves the door open for the Secretary of State to recommend a new public interest criterion in an area where no merger has yet been proposed.

Indeed, it is this lack of detailed guidance on how, and when, section 58(3) is to be applied which makes it such a dangerous provision. As the public interest is an abstract concept, the activities considered to be in the public interest are subject to change. Over time, certain interests may become more socially or economically significant and, as a consequence, they may create extreme circumstances in certain merger transactions. Section 58(3) may well afford the Secretary of State the flexibility to address these new problems, but it may also create an undesirable trend of new public interest exceptions being introduced via the back door.

If we accept that public interest criteria have a place in UK merger control, however restrained the definition, then we should give serious thought to how we can best accommodate them without undermining the certainty and robustness of the merger regime as a whole. Although the Government has avoided the issue under the latest reforms, we need a thorough debate on which public interests warrant specific protection and whether merger control can provide this protection effectively. Equally, we need a review of who should be making the final decision in public interest mergers. Given the new potential for the CMA to consider public interest concerns in market investigations under the ERRA13, it is clear that the Government appreciates the ability of the CMA to assess wider social issues. A decision-making committee – encompassing the Secretary of State and the CMA – is an interesting idea and one that might go some way towards ensuring that competition and public interest concerns are each afforded the consideration they warrant. Certainly, we should not assume that public interest mergers are off the political agenda indefinitely.

2: The duty to make a reference is derived under the EA02: section 22(1) for completed mergers, and section 39(1) for anticipated mergers.
3: As specified under sections 58(1) and 58(2A)-(2C) EA02 respectively.
4: The Secretary of State derives this power under section 42(2) EA02.
5: HL Deb 18 July 2002 vol 637 cc1488, 1498.
11: HL Deb (n 6) cc1488, 1490.
12: Consider, for example, the stance adopted by France’s Markets Regulator: Anousha Sakoui, Anne-Sylvaine Chassany and James Boxell, ‘French agency eyes tougher merger rules’ Financial Times (London, 4 March 2013). Available at: www.ft.com/cms/s/0/6a4e11e4-84f3-11e2-891d-00144feabdc0.html#raccz2PGkC9sM6.
Our 2013 Summer Conference – ‘Institutions and Competition Policy’ – was intellectually stimulating and a lot of fun, providing us with two days of engaging and lively debate on the structure of enforcement institutions. A report of the conference can be found in this Bulletin. Warm thanks are extended to all of our delegates and our excellent speakers. You can catch up online, where a video of our speakers highlighting key points from their presentations is available. http://competitionpolicy.ac.uk/summer-conference-2013

Naturally, we are now looking forward to our 10th Annual Conference next summer, which will focus on ‘Problem Markets’ - those markets that generate media attention, that don’t seem to be working for consumers and provide competition agencies with headaches. Our conference will be looking at the economic factors behind such markets and will consider which institutional and legal frameworks are appropriate for dealing with them.

After 9 years in offices in the iconic Ziggurats, with their superb views over the University Broad, and 3 months in a shared temporary space, we have now settled into offices on the top floor of the Elizabeth Fry building on the UEA campus. Anyone planning a return visit to CCP, please note this change.

Nothing stands still at CCP, and in addition to the office move this summer, we have been pleased to welcome the following new Research Associates: David Deller, Joo Young Jeon, Antje Kreutzmann-Gallasch, Hao Lan and Francesca Vantaggiato. Furthermore, two RAs have moved on, but not too far: Miguel Flores is now a Post-Doctoral Research Fellow at CCP and Sven Gallasch a Lecturer in the UEA Law School. Sven joins two new faculty members, Andrea Patacconi [NBS] and Sang-Hyun Kim [Economics]. Also, several members have left CCP: Sebastian Peyer and Tong Wang have left positions as Post-Doctoral Research Fellows for lecturerships at the University of Leicester School of Law and the University of Edinburgh Business School respectively. Finally, faculty members Pinar Akman and Peter Whelan have joined the University of Leeds School of Law. Our best wishes go to them all.