UK Merger Remedies under Scrutiny

October 2006

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CCP Policy Briefing

INTRODUCTION

- With a focus on a recent Competition Appeal Tribunal (CAT) case, *Somerfield v Competition Commission* [2006] CAT 4, this paper explores the problems faced by competition agencies in scoping divestiture remedies.
- Despite new merger remedies guidelines issued by the EC and US in 2001 and 2004 respectively, and significant reform of Europe's merger control regime, the question of the efficacy of merger remedies is a matter of current concern in legal and policy circles.
- There are two main strands to the concerns over merger remedies:
    - That competition agencies have often acted strategically, imposing remedies which go beyond that which is necessary to correct the anti-competitive effects of the mergers in question;
    - That the merger remedies imposed are not sufficiently effective given the potential for strategic action on the part of merging parties and the informational asymmetries which exist as between the parties and the agencies.

MECHANICS OF US AND EC MERGER CONTROL

- In both the US and the EC, mergers which meet certain jurisdictional thresholds must be notified to and scrutinised by the relevant competition authority. In the UK, however, the merger regime does not provide for the compulsory notification of mergers, although transactions which are not notified may be subject to an *ex post* investigation and remedies.
- Broadly speaking, the EC, US and UK merger regimes are all organised around two investigatory phases. In the UK, remedies can be imposed at the end of either stage.

AGENCY GUIDELINES ON MERGER REMEDIES

- The UK Competition Commission's guidelines express a presumption in favour of divestment as a remedy; such an approach ordinarily involves a "clean break", without the need for continued supervision. In the US and the EC this approach has been approved by both the US Supreme Court and the EC Court of First Instance.
- According to its guidelines, the Competition Commission, when choosing between two equally effective remedies, will choose the one that is least expensive or least restrictive. However, where a remedy is imposed post-transaction, the agency will not generally have regard to the parties' implementation costs.

EFFICACY OF MERGER REMEDIES

- An FTC study (1999), and a DG Comp study (2004), into the success of divestment packages and the effectiveness of merger remedies, underlined the importance of ensuring that the assets divested represented a viable ongoing business. Buyers were at a potential "substantial disadvantage", both in respect of information and of bargaining power, as compared to sellers.
- In practice there was found to be systematic bias on the part of the sellers in favour of divesting to the weakest purchasers. Buyers did not perceive themselves to be in a strong bargaining position, and tended not to inform the agency when having problems

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negotiating a satisfactory package. Both the FTC study and the DG Comp study concluded that there was a need for more systematic supervision of remedies *ex post*. The DG Comp study also underlined the importance of scrutinising the motivations of purchasers.

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JUDICIAL REVIEW OF MERGER REMEDIES

- In *Somerfield v Competition Commission* the CAT was faced with two key issues:
  - Whether the Commission was entitled to require the divestment of *acquired* stores rather than *existing* stores: Somerfield argued that they should have a free choice of which stores to divest because the 'substantial lessening of competition' (SLC) identified by the Commission to be remedied was caused solely by the common ownership of existing and acquired stores. The Commission, on the other hand, claimed that it was entitled to require divestment of the stores most likely to restore the SLC in a timely fashion.
  - The extent to which the Commission was entitled to restrict the pool of potential divestees, an issue crucial to the question of whether a suitable purchaser would be found: Somerfield cited the Commission's identification of a competitor set which comprised those firms that acted as a significant competitive restraint on Somerfield stores as "perverse".
- Broadly speaking, the CAT upheld the approach of the Commission. In accordance with its guidelines, it was entitled to require divestment of assets which were most likely to restore competition in the most timely and certain manner. In the course of its judgment, the CAT also made a number of observations over the onus and standard of proof relating to merger remedies. For example, the Commission was afforded a "margin of appreciation" commensurate with the expertise of its membership. The CAT further stated that the "onus is on Somerfield to show that the [Commission] could not reasonably have come to the conclusion that it did, and not on the [Commission] to show that it had grounds for depriving Somerfield of a choice of store" to divest.

CONCLUSION

- Since the publication of the FTC and DG Comp studies, it has been clear that the seller of divestment packages will often have strong incentives to undermine the remedial outcome. In this case, Somerfield was seeking to dispose of its least attractive assets to its least effective competitors. The CAT was right, therefore, in showing an appropriate degree of deference to the Commission, and it is likely that UK merger remedy packages will be more effective as a result.

THE CCP

The ESRC Centre for Competition Policy (CCP), at the University of East Anglia, undertakes competition policy research, incorporating economic, legal, management and political science perspectives, that has real-world policy relevance without compromising academic rigour.

FOR MORE INFORMATION

The full working paper (CCP Working Paper 06-16) and more information about CCP and its research is available from our website: www.ccp.uea.ac.uk

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