

CMA impact assessment 2015/16

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1. Summary

- 1.1 The Competition and Markets Authority (CMA) is the UK's lead competition and consumer authority and its primary duty is to promote competition, both within and outside the UK, for the benefit of consumers. It is an independent non-ministerial government department which, from 1 April 2014, brought together and took on the functions of the Competition Commission (CC) and many of the functions of the Office of Fair Trading (OFT). The CMA has a wide range of tools to use in addressing competition and consumer problems including carrying out investigations into mergers and markets, enforcing competition and consumer law and working with sector regulators. The CMA also has a function to consider regulatory references and appeals.
- 1.2 As part of its performance framework agreement with the Department for Business, Innovation and Skills (BIS)¹ the CMA is required to report annually on:
 - (a) the delivery of a target of direct financial benefits to consumers of at least ten times its relevant costs to the taxpayer (measured over a rolling three-year period); and
 - (b) the ratio of direct financial benefits to consumers and costs for its principal tools.
- 1.3 In this second CMA impact assessment we report on performance against this target for the financial year 2015/16.
- 1.4 As the target is measured as a three-year rolling average, for 2015/16 the calculation is based on the performance of the final year of the OFT and CC and the first two years of the CMA. The assessment is undertaken by the CMA itself and is reviewed by an external academic. This year the academic was Professor Stephen Davies of the University of East Anglia. The methodology used by the CMA is based on that developed and used by the OFT and CC, validated by successive independent academic reviewers and consistent with approaches now regarded by the OECD as international good practice.² However, there are some areas of difference between the OFT's and the CMA's methodologies. These are highlighted in Section 2 below.
- 1.5 For the period 2013 to 2016 the estimated average direct financial benefit to consumers was £686.8 million per annum and the ratio of direct benefits to

¹ BIS (January 2014), *Competition and Markets Authority: performance management framework*.

² OECD (April 2014), *Guide for assessing the impact of competition authorities' activities*.

cost was 10.6. The breakdown of the financial benefit by tool is set out in Table 1 below.

Table 1: Estimated average annual CMA/OFT/CC consumer savings and costs for 2013–16

	<i>£m</i>
<i>Area of CMA work</i>	<i>Savings</i>
Competition enforcement	73.6
Consumer protection enforcement	74.1
Merger control*	16.4
Market studies and market investigations	522.7
<hr/>	
Total benefits	686.8
Costs	65†
Benefit/costs	10.6:1

*The CMA has a duty to investigate mergers that legally qualify for scrutiny. This means that CMA merger control work is demand-led and not discretionary, unlike most other areas of the CMA's work. Given that the number of qualifying mergers can vary considerably from year-to-year (because of fluctuations in the economic cycle for example), the number of investigated mergers and the direct consumer benefits of the CMA's merger control work can also vary significantly from year-to-year.

†This is total CMA costs (actual spend) minus costs of the CMA work on regulatory appeals.

1.6 Our benefit estimates necessarily rely in part on assumptions.³ In general, the assumptions we apply are cautious and hence we consider our estimates to be conservative.

1.7 The CMA often works with other regulators or provides input for the work of other regulators to make markets work well and generate benefits to consumers within and outside the UK. We claim impact from the work of other regulators only where the CMA has made a significant contribution or has taken a leading role. For example, our benefit estimates for 2015/16 include impact from the rulings of the Advertising Standards Authority (ASA) in relation to children's online games⁴ which followed referrals by the CMA⁵ and impact from the European-wide consumer protection project in relation to short-term car rental led by the CMA.⁶

1.8 Our estimates exclude impact from a number of cases where the CMA's intervention is likely to generate substantial consumer benefits but these benefits were difficult to quantify in a sufficiently robust manner. An example of this for the financial year 2015/16 is the CMA's consumer protection work in the higher education sector.⁷ We also excluded cases where the impact of the CMA's work depends on the actions of policymakers and regulators and it is not yet clear whether the CMA's recommendations will be accepted. For this reason we did not include in our assessment the CMA's competition policy

³ Impact estimations are conducted immediately after cases are completed and are therefore based only on information available during the case and on assumptions regarding the expected impact of our interventions. On this basis the estimates are considered to be 'ex ante' evaluations.

⁴ [ASA Ruling on Mind Candy Ltd](#); [ASA Ruling on 55 Pixels Ltd](#).

⁵ CMA press release (2015), '[CMA refers three children's online games to the ASA](#)'.

⁶ CMA press release (2015), '[Car rental customers set to drive off with better deals](#)'.

⁷ CMA case: [Higher education: consumer protection review](#).

project in relation to passenger rail services;⁸ our report published in March 2016 contained recommendations which the government has welcomed and agreed to explore how to implement,⁹ but which have not yet been implemented. We will assess the impact attributable to this project when the government's intentions, and their likely impact, become clearer.

- 1.9 The estimate of benefits excludes the CMA's compliance work,¹⁰ international activities¹¹ and advocacy to government for policies that support competition because the benefits of these, whilst substantial, can be difficult to quantify due to the nature of the work. We also exclude regulatory appeals as our role is an appellate one rather than being the primary regulator.¹²
- 1.10 In addition, the focus on direct financial benefits means that we exclude many important wider impacts of the competition regime. For example, we do not take into account the deterrence effect of our work, such as the deterrence of anti-competitive mergers or anti-competitive conduct. Evidence from existing academic studies¹³ and previous OFT research¹⁴ indicates that such deterrence is significant albeit very difficult to measure. Studies also show that increases in competition in a market are often associated with increases in productivity, and that competition policy interventions can therefore improve productivity.¹⁵ This impact on productivity is not captured in our impact assessment. In sum, evidence suggests that the direct impact of interventions is only a part of the overall impact of competition authorities' work. In order to gain a better understanding of the overall impact of our work and deterrence in particular, we will continue to do and encourage research and analysis in this area.

⁸ CMA case: [Passenger rail services: competition policy project](#).

⁹ UK Parliament (2016), [Rail Reform: Written statement - HLWS609](#).

¹⁰ See for example the CMA's compliance activity in relation to property sales and lettings following an infringement decision ([Property sales and lettings investigation](#)). While it is reasonable to believe that the infringement decision and the follow-up compliance work have had an impact on the behaviour of businesses outside the scope of the original investigation, we do not include this wider impact in our estimates.

¹¹ Eg in 2015/16 the CMA was the president of the International Consumer Protection and Enforcement Network. Our impact estimates do not account for benefits from this work.

¹² Our duty in this area is to act according to the relevant legal framework rather than necessarily acting in the immediate interest of consumers.

¹³ Some of these studies were presented at the conference organised by the CMA, the European Commission and the Netherlands Authority for Consumer and Markets on the indirect impact of competition authorities' work in September 2015: [Indirect impacts of competition authorities' work: conference presentations](#).

¹⁴ See *The impact of competition interventions on compliance and deterrence*, OFT1391 and *The deterrent effect of competition enforcement*, OFT 962.

¹⁵ CMA (2015), [Productivity and competition: a summary of the evidence](#).

2. Overview of our methodology

- 2.1 The CMA conducts both impact estimates (ex-ante evaluations) and detailed long-term evaluations (ex-post evaluations) to estimate the impact of our work. Ex-ante estimates of impact are based on the best information available at the time of estimation – which is typically when the decision or recommendations have been made or implemented but the full impact is not yet observable. Ex-post evaluations are more robust and are based on information gathered after the recommendations/remedies have been implemented and the resulting impact realised, often several years after the case has been completed. Ex-post evaluations are only conducted for a small subset of cases – at least two a year. The most recent of these ex-post evaluations, published in May 2016, looked at the Competition Commission’s 2009 market investigation into BAA airports.¹⁶ The figures presented in Table 1 are derived from ex-ante impact estimates made shortly after the completion of cases.
- 2.2 The methodology used when preparing the estimates for the CMA’s impact assessment reports, including this one, is largely consistent with that previously used by the OFT for its annual positive impact assessments¹⁷ and by the CC in its impact assessment work. However, there is one important area of difference. Unlike the OFT positive impact report, the CMA impact assessment estimates include benefits from cases where the outcome is under appeal at the time of publication of the report. We include these benefits as we consider this ensures the impact assessment is the best estimate of the likely impact of the CMA cases at the time of the publication of the report. In addition, this approach also ensures that the benefit estimates are included in the impact assessment at roughly the same time as the costs the CMA incurred in carrying out the case.¹⁸ This approach requires that subsequent impact assessments may need to be revised to take into account the outcome of any appeals. No adjustment of this nature had to be made with respect to the CMA’s 2014/15 impact assessment.
- 2.3 Given the CMA’s primary duty to promote competition, both within and outside the UK for the benefit of consumers, the impact estimations included within this report focus on the direct financial benefits to consumers of the CMA’s work. The direct financial benefits to consumers may include, for example, the direct reduction in prices to consumers or the value to consumers of

¹⁶ CMA case: [BAA Airports: evaluation of remedies](#).

¹⁷ Past OFT assessments can be found on [The National Archives’ website](#).

¹⁸ It can be several years before appeals are concluded leading to a significant lag between the inclusion of the benefits and costs of certain cases.

improvements in quality, service or information provision following an intervention.

- 2.4 Many of the beneficial outcomes of the CMA's work are not easily quantifiable and are not included in the total benefits shown in Table 1. For example, these figures do not attempt to measure the deterrence effect of our work in the areas of merger control and competition and consumer enforcement, or the impact of increased competition on innovation, productivity or economic growth. As discussed in paragraph 1.10, each of these can be significant. In addition, the estimate of benefits does not encompass the full extent of the CMA's work as the impact of international and compliance work and advocacy are excluded from our impact assessment.
- 2.5 We use the Consumer Price Index to take account of inflation. In line with central government techniques for discounting future accruals of benefits or costs, we discount future consumer savings by the HM Treasury endorsed Social Time Preference Rate (3.5%).¹⁹

¹⁹ See HM Treasury, *The Green Book: Appraisal and Evaluation in Central Government*.

3. Consumer savings by area

Introduction

- 3.1 This section presents estimates of the impact of our work for each of the following areas: enforcement of competition law, enforcement of consumer protection legislation, merger control and markets work.
- 3.2 For merger control and markets work, the CMA is both the phase 1 and phase 2 authority in a two-stage process (phase 1 cases being referred where there are sufficient competition concerns to require further, more in depth, phase 2 investigation). Although the decision makers at phase 2 comprise a group of independent members drawn from the CMA panel (to ensure a transparent and distinct process) the CMA has responsibility for both phases including their resourcing. Where cases have been referred to phase 2 benefit estimates are only made once the phase 2 process has been completed although both phase 1 and phase 2 costs are part of the impact assessment.
- 3.3 We do not publish impact estimations for individual cases. Case estimates have been independently reviewed by Professor Stephen Davies²⁰ to ensure that our benefit estimates are reasonable and robust.

Competition enforcement

- 3.4 The CMA engages in a range of activities aimed at ensuring compliance with the Competition Act 1998 (CA98), including formally investigating and taking enforcement action against anti-competitive practices and using ‘softer’ tools such as providing guidance and targeted compliance initiatives.²¹ Under the Enterprise Act 2002 (EA02) we can also investigate and prosecute individuals who have committed a cartel offence.
- 3.5 We estimate that the CMA’s (and previously the OFT’s) interventions saved consumers at least £220.9 million in aggregate between the financial years 2013 and 2016 representing annual average consumer savings of £73.6 million. These savings are typically derived from price reductions that are likely to follow the break-up of a cartel or from stopping other unlawful conduct.
- 3.6 The estimate does not include the significant deterrent effect of our competition enforcement actions. In 2011 the OFT published deterrence ratios

²⁰ Stephen Davies is Professor of Economics at the University of East Anglia.

²¹ The benefits from these softer tools are not typically included in the quantified estimate of benefits.

for its competition enforcement work, produced by London Economics.²² The research estimated that for each cartel case investigated by the OFT, 28 others were deterred.²³ For investigations into abuse of dominance and other commercial agreements, the figures were 12 and 40 cases deterred respectively. The overall magnitude of the CMA's impact is therefore expected to be significantly higher than the estimated direct financial benefits.

Consumer protection enforcement

- 3.7 The CMA's consumer protection enforcement work seeks to change trader behaviour that appears to contravene consumer protection legislation using a range of interventions such as publishing guidance, issuing informal warnings, accepting undertakings under the EA02, or obtaining court orders.²⁴ All interventions are aimed at protecting consumers, particularly vulnerable consumers, from rogue trading, unfair commercial practices and other breaches of consumer protection legislation. The CMA has taken over some, but not all, aspects of the consumer protection work of the OFT. The main powers which transferred to other agencies are those conferred by the Consumer Credit Act 1974²⁵ and the Estate Agents Act 1979.²⁶ OFT powers under anti-money laundering legislation have transferred along with these statutory functions.²⁷
- 3.8 For the period 2013 to 2016, the total consumer benefits in aggregate from relevant consumer enforcement work are estimated to be £222.3 million, giving an average of £74.1 million per year. These benefits may include a reduction in consumer detriment as a result of stopping unlawful practices or the estimated price impact of the CMA's interventions, for example, as a result of increased transparency and more informed consumer decisions. Our estimates, however, do not include the deterrence effect of the CMA's consumer protection activities. In addition, as mentioned in paragraph 1.8, we

²² See *The impact of competition interventions on compliance and deterrence*, OFT1391. The research identifies and quantifies the wider benefits and costs associated with deterrence resulting from enforcement activities undertaken by the CMA and previously by the OFT.

²³ There are also a number of academic studies showing that competition authorities' cartel enforcement activities have a significant deterrence effect. See eg Clarke, J.L. & S.J. Evenett (2003), 'The deterrent effects of national anticartel laws: evidence from the international vitamins cartel', *Antitrust Bulletin*, Vol. 48, No. 3, pp689–726; Smuda, F. (2013), 'Cartel Overcharges and the Deterrent Effect of EU Competition Law', *Journal of Competition Law & Economics*, Vol. 10, No. 1, pp63–86. We are not aware of any academic papers focusing on the deterrence effect of other areas of competition enforcement such as investigations into abuse of dominance or anti-competitive vertical agreements.

²⁴ Trading Standards are also responsible for consumer protection enforcement and tackling unfair trading practices. This section only considers the consumer savings resulting from CMA and past OFT enforcement action. For an evaluation of the activities of Trading Standards, see OFT (June 2009), *An evaluation of the impact of the fair trading work of local authority Trading Standards Services in the UK*, OFT1085.

²⁵ To the Financial Conduct Authority.

²⁶ To the National Trading Standards Estate Agency Team.

²⁷ The CMA's role in consumer protection is set out in more detail in our [consumer protection guidance](#).

do not include cases in our impact assessment where benefits cannot be quantified in a sufficiently robust manner, for example, because of the nature of the changes expected in the market or data availability issues. This was the case for the CMA's consumer protection work in relation to the higher education sector.²⁸ While the CMA's work is likely to bring significant benefits to students as a result of more-informed decisions, we did not have sufficient data and information to estimate these benefits. Therefore, the impact of the CMA's consumer protection work is likely to be significantly larger than the £74.1 million (average) annual benefit we quantified.

Merger control

- 3.9 The CMA operates both stages of the UK two-stage merger regime. Businesses can (voluntarily) notify a merger to the CMA and, in addition, the CMA has a duty to keep merger activity under review and can investigate mergers that have not been notified to it. At phase 1 it reviews merger situations falling within its jurisdiction²⁹ and refers for more detailed scrutiny (at phase 2) any cases where there is a realistic prospect of a substantial lessening of competition (SLC) in a UK market. The CMA has the power to accept undertakings in lieu (of reference to phase 2) (UiL) from the merging parties, if these are deemed to address potential concerns identified in the course of its investigations.
- 3.10 At phase 2, a CMA panel of independent members conducts an in-depth investigation to assess if a merger is expected to result in an SLC. If an SLC is expected, the CMA decides upon the remedies required and can impose remedies by order if it is not able to agree them with the businesses.
- 3.11 Our estimates of consumer savings in this area include merger proposals amended through UiLs, mergers that are abandoned on referral to phase 2 (abandoned mergers), and mergers amended or prohibited by the CMA at phase 2.
- 3.12 The estimates for abandoned mergers and UiLs have been scaled down by the 'SLC rate'. The SLC rate is the proportion of the mergers over the period 1 April 2013 to 31 March 2016 examined at phase 2 where an SLC finding was made; it is currently 36%. This methodology is consistent with that used by the OFT and it is applied to account for the uncertainty of the outcome of a phase 2 reference. We consider that this scaling down leads to very

²⁸ CMA case: [Higher education: consumer protection review](#).

²⁹ Mergers of businesses with EU and global turnover above a certain size fall within the jurisdiction of the European Commission. Mergers affecting trade between member states may also be reviewed by the European Commission.

conservative estimates for phase 1 merger benefits as it assumes that those mergers where UiLs are offered would be cleared with the same probability in phase 2 as those where UiLs were not offered. Therefore, we will review this methodology for the first CMA-only impact assessment next year.

- 3.13 Using the approach described above, our estimates show that during the past three financial years (2013 to 2016) the merger regime has saved consumers £49.1 million in total, giving an average of £16.4 million per year.
- 3.14 The benefits from the UK merger regime are dependent on the cases that come to the CMA for assessment and are therefore driven, in part, by the economic climate and can vary significantly from year to year. They are also dependent on the composition of the merger being assessed. If anti-competitive mergers are proposed and prohibited or altered then the estimated direct benefits of the merger regime will be greater. Our estimates exclude benefits from mergers affecting UK consumers which are reviewed by the European Commission.³⁰
- 3.15 Benefit figures for mergers do not include the wider benefits, such as deterrence, of its mergers work and the wider merger regime, which we would expect to be significant. In 2007 the OFT published deterrence ratios for our mergers work, produced by Deloitte.³¹ The survey suggested that at least five proposed mergers were abandoned or modified on competition grounds before the OFT became aware of them for each one merger blocked or modified following intervention by the UK competition authorities. Academic studies also show that the harm avoided by blocking anti-competitive mergers or clearing mergers with remedies is likely to be just a fraction of the overall harm deterred by merger control.³²

Market studies and market investigations

- 3.16 Market studies are examinations into the causes of why particular markets appear not to be working well for consumers and may lead to proposals as to how they might be made to work better. They take an overview of regulatory and other economic drivers in a market and patterns of consumer and business behaviour.

³⁰ See previous footnote.

³¹ See OFT (November 2007), *The deterrent effect of competition enforcement by the OFT*. Note that this analysis is not directly comparable with the more recent deterrence work conducted for the OFT by London Economics (published December 2011).

³² Eg Seldeslachts, J., J.A. Clougherty & P.P. Barros (2009), 'Settle for Now but Block for Tomorrow: The Deterrence Effects of Merger Policy Tools', *Journal of Law and Economics*, Vol. 52, No. 3, pp607–634.

- 3.17 Markets may be referred for a market investigation for further analysis where there are reasonable grounds for suspecting that any feature, or combination of features, of a market in the UK is preventing, restricting, or distorting competition. In estimating consumer savings we consider the impact of both market studies that have not resulted in a market investigation and completed market investigations.
- 3.18 Where the market study or review makes recommendations to other government departments or regulators, we assess impact for the CMA's intervention when it is reasonable to believe that those recommendations will be accepted.³³ Where the market study or review has led to action by other government departments or regulators following our recommendations, we only attribute a proportion of the impact to the CMA. For example, where CMA recommendations are implemented by another government department, the impact estimates are apportioned between the CMA and the relevant government department.
- 3.19 We estimate that the savings from the markets regime are £522.7 million per annum between the financial years 2013 and 2016.³⁴

³³ For this reason we did not include in our assessment the CMA's competition policy project in relation to passenger rail services ([Passenger rail services: competition policy project](#)). Our report published in March 2016 contained recommendations which the government has welcomed and agreed to explore how to implement. We will assess what impact can be attributed to this project as and when the government's intentions, and their likely impact, become clearer.

³⁴ Apart from the policy project in relation to passenger rail services, no market study or market investigation was completed in the financial year 2015/16. The CMA's markets work in this period principally comprised the major two-year duration market investigations into the energy and retail banking markets. As we have not included any impact in 2015/16 in relation to the rail project, the benefits from markets work for the financial year 2015/16 alone are zero.

4. Costs

- 4.1 Cost figures may fluctuate from year to year and as such will have an impact on the benefit to cost ratios reported in the CMA impact assessment. To smooth out any such fluctuations, we use a three-year moving average for total costs. This is consistent with the way in which we report estimated benefits.
- 4.2 For the purposes of calculating the benefit to cost ratio, the total costs of the CMA for the financial years 2014/15 and 2015/16 exclude the costs incurred in fulfilling the CMA's function with regard to the determination of regulatory appeals as we do not include any benefits from these in the impact assessment. For the financial year 2013/14 the costs are those of the OFT and the CC.³⁵ The CC costs are the total net CC cost as reported in the annual accounts.³⁶
- 4.3 On this basis, the average annual CMA/CC/OFT costs over the financial years 2013 to 2016 is estimated at £65 million.³⁷

³⁵ The OFT costs exclude those related to consumer credit licensing and related anti-money laundering activity because the OFT was not required to conduct impact estimation.

³⁶ This will tend to have a downward impact on the benefit-cost ratio as we have not removed cost for activities for which we do not estimate corresponding benefits, such as regulatory appeals.

³⁷ Figure in March 2015 prices.