Exceptions to the duty to refer

Summary of responses to the consultation

13 December 2018
CMA64

Contents

Page

1. Introduction

Background

1.1 The Competition and Markets Authority (CMA) is the UK's primary competition and consumer authority. The CMA works to promote competition for the benefit of consumers, both within and outside the UK, to make markets work well for consumers, businesses and the economy.

1.2 The CMA is introducing new guidance to explain its approach in relation to exceptions to the duty to refer a merger for a phase 2 investigation. This follows a consultation, which ran from 12 June 2018 to 20 July 2018, on a draft of that guidance.

1.3 The guidance seeks to update and consolidate guidance on exceptions to the duty to refer. It supersedes Mergers: Exception to the duty to refer in markets of insufficient importance (CMA64)[1], and Chapters 1, 3 and 4 of Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance (OFT1122)[2].

1.4 The approach outlined in the guidance is consistent with these previous documents, but has been updated and extended to take account of the CMA's experience of merger investigations in recent years.

Purpose of this document

1.5 The CMA's consultation set out three questions on which respondents' views were sought:

(a) Is the content, format and presentation of the draft guidance sufficiently clear? In particular, does the draft guidance clearly explain the relationship between RCBs and remedies? If there are particular parts of the guidance where you feel greater clarity is necessary, please be specific about the sections concerned and the changes that you feel would improve them.

---

[1] Mergers: Exceptions to the duty to refer in markets of insufficient importance (CMA64)

[2] Mergers: Exceptions to the duty to refer and undertakings in lieu of reference guidance (OFT1122) was originally published by the OFT and was adopted by the CMA. In relation to markets of insufficient importance it was replaced by CMA64. Guidance on undertakings in lieu of reference (previously in Chapter 5 of OFT1122) is now included in the new guidance on merger remedies which is being published simultaneously with this guidance on exceptions to the duty to refer.

(b) Is the draft guidance sufficiently comprehensive? In particular, does the it provide enough examples of the type of evidence that the CMA requires in its assessment of RCBs? Does it have any significant omissions? Do you have any suggestions for additional or revised content that you would find helpful?

(c) Do you have any other comments on the draft guidance?

1.6 This document is intended to summarise the key issues raised by the responses and the CMA's views on these key issues. It is not intended to be a comprehensive record of all views expressed by respondents (respondents' full responses are available on the consultation page). This document should be read in conjunction with the consultation document, which contains further background and explanation on the new guidance.

2. Issues raised during the consultation and our response

2.1 The CMA received six written responses to the consultation. The list of respondents is at Appendix A, and non-confidential versions of all submissions are available on the consultation page.

2.2 Respondents generally considered that the draft guidance was clear, in terms of content, format and presentation. Summaries of responses are set out below, together with the CMA's views on the comments in question.

2.3 We have taken into account requests for clarification in the guidance.

Markets of insufficient importance

Respondent views

2.4 Respondents made the following comments and suggestions in relation to markets of insufficient importance to justify a reference:

(a) The Enterprise Act 2002 should give the CMA a general discretion to refer rather than a duty to refer, particularly in the light of the UK's exit from the European Union (**Brexit**). (One respondent.)

(b) Given the significant increase in the CMA's mergers workload anticipated as a result of Brexit the CMA should consider increasing the *de minimis* thresholds in order to focus resources on large complex global transactions. (Three respondents.)

While the consideration of *de miminis* issues at an earlier stage in the investigation (and in particular as part of the decision on whether to call in a merger for review) has had a positive impact, it remains the case that the UK merger regime catches too many inconsequential mergers and that this results in an inefficient use of the CMA's resources given the CMA's target of delivering direct financial benefits to consumers of at least ten times its relevant costs to the taxpayer.

The application of the current de minimis thresholds in many cases serves only to deliver direct financial benefits to consumers in the form of lower prices that are broadly equal in value to, or only marginally more than, the cost to taxpayers of a phase 2 reference. Applying the CMA's target of taxpayer value more rigorously would imply a threshold (at least for mergers involving national markets) of closer to £50 million, rather than £5 million. The CMA should make formal commitment to review the

thresholds periodically (every three years) and/or index link them to make sure they remain appropriate. (One respondent.)

(c) CMA should use this consultation as an opportunity to increase the current *de minimis* thresholds. The current levels of £5m and £15m are low, and as a result, the CMA is still able to review relatively small mergers. In our view, the CMA should not have jurisdiction to review mergers where the value of the market concerned is less than £15 million. Alternatively, the parties should be able to submit a short letter to the Mergers Intelligence Committee explaining why the de minimis exception should apply. This would enable the CMA to decide whether to apply the exception before starting a Phase 1 review. If the CMA determines that the exception applies, it would inform the parties at the outset that it will not call in the merger, thus eliminating the need for a merger filing. (One respondent.)

(d) One respondent states that in Germany de minimis markets (that is, concentrations exclusively affecting a market in which goods or commercial services have been offered for at least five years and which had a market volume of less than €15 million in the last calendar year), are exempt from substantive review but must be notified. This respondent suggests that it may be worth considering whether the five-year limb of the German test adds value in ensuring that novel or developing markets are not exempted from the ex ante review prematurely, and that this could be one of the considerations for the duration of the SLC.

(e) Where the annual value in the UK of the market concerned is £5m - £15m, the CMA says it will consider whether the expected customer harm resulting from the merger is materially greater than the average public cost of a Phase 2 reference, which it estimates to be around £400,000. The figure of £400,000 has not changed since the OFT's 2003 Substantive Assessment Guidance, which is surprising. Given that Phase 2 investigations have become more transparent since 2003 and more document-intensive, we would expect that figure to have increased. We consider that the de minimis thresholds should be set by reference to an updated estimate of the cost to the public of a Phase 2 reference, which we suspect has increased since 2003. (One respondent.)

(f) Footnote more recent merger cases to provide examples to the points made in the guidance, including referencing those that have been decided since the guidance was revised last year. (One respondent.)

(g) The CMA should continue to consolidate its guidance documents, to ensure consistency and enable greater accessibility to the CMA's practice

which, at present, can occasionally be difficult to discern for practitioners without a background in competition law. (One respondent.)

(h) One respondent requested examples or illustrations of the factors that would be taken into account to estimate the duration of the SLC, for example, whether the CMA would consider barriers to entry.

(i) While the draft guidance specifies in paragraph 36 that overall market is calculated based on the turnover of all parties, which is helpful, it would be better to set this out at the beginning. The parties will have their own turnover figures but may in certain instances struggle to find turnover data of competitors to estimate the overall value of the annual UK market. Please say what evidence the CMA would accept for this purpose. (One respondent.)

(j) One respondent felt that the CMA should have used the consultation to provide more comment on its approach in the past few years. This respondent suggested, by reference to one case, Capita/Vodafone, that the CMA should take the counterfactual submitted by the parties into account when weighing the costs of a Phase 2 reference against the importance of the market. The CMA was not persuaded by Vodafone's claims that it would have exited the market but for the merger, and therefore did not adopt this as an appropriate counterfactual for its merger analysis. Furthermore, the CMA did not return to the possibility that Vodafone would exit the market if a CMA reference was made when considering whether the market was of insufficient importance for a reference. The respondent claims that Vodafone immediately terminated its paging business following the reference, causing avoidable disruption to customers and suggests that it may, in certain circumstances, be appropriate for the CMA to consider the parties' own proposed counterfactual when assessing the question of its duty to refer.

CMA response

2.5 The CMA’s response to the points above is as follows:

(a) There is already a discretion whether to refer in relation to markets of insufficient importance, undertakings in lieu of reference and transactions insufficiently far advanced or insufficiently likely to proceed. The CMA notes the suggestion that there should be a wider discretion not to refer even if none of these exceptions apply. However, this is outside the scope of the current consultation.

(b) The CMA notes that the market size thresholds at which markets are considered to be of insufficient importance to justify a reference are one of the means which could be used to manage the number of cases post-Brexit. However, it may be more appropriate to consider such an adjustment once the impact of Brexit on competition in the UK and on the CMA's workload is clearer. For example, if Brexit leads to a slackening of competitive pressure from continental European competitors then small markets with limited numbers of domestic participants may continue to be of interest from a merger control perspective.

(c) The CMA disagrees with the suggestion that it should not have jurisdiction to review mergers where the value of the market concerned is less than £15 million.

First, this would require a statutory amendment, which is outside the scope of the consultation. Secondly, the exception relates to the importance (including size) of the market, not the size of the merger.

Thirdly, irrespective of the size of the market, it is appropriate to consider whether to review a merger if it appears that it may lead to a substantial lessening of competition (**SLC**). For example, nascent technologies may currently involve small market size but be of sufficient importance to warrant a reference. Market size is just one factor in deciding whether a market is of sufficient importance to refer. The £5/15m figure was carefully considered in 2016. However, as indicated under (b) above the CMA is open to reviewing it once the impact of Brexit is clearer.

Finally, as indicated at paragraphs 53-55 of this guidance, the CMA does consider any submission relating to the importance of the market before calling a merger in. Such submissions can be made in accordance with the Guidance on the CMA's mergers intelligence function (CMA56). However, it would be inappropriate to give a firm commitment not to call a case in without a full review, since doing so would create an extra-statutory clearance procedure.

(d) The CMA agrees that it is important not exempt markets from reference purely on the basis of the turnover currently generated in the market. The CMA agrees that the fact that a market is nascent or rapidly developing is a factor that can be taken into account in assessing the durability of the mergers impact. A sentence has been added to paragraph 50 to highlight this. The exception for markets of insufficient importance as currently drafted seems preferable to thresholds linked to a specific period of years and a specific turnover as rigid rules might result in arbitrary and undesirable outcomes.

(e) The Figure of approximately £400,000 for the public cost of a typical phase 2 investigation was considered and confirmed in the CMA's 2016 review of the guidance on markets of insufficient importance. For example, the cost per investigation has been kept down by merging the Office of Fair Trading and Competition Commission. While the public cost of phase 2 investigations does not necessarily increase in line with the cost to the parties, the CMA notes the need to review this figure periodically.

(f) Footnotes to more recent cases have been added throughout the section on markets of insufficient importance, in particular at paragraph 21.

(g) The CMA will continue to strive to make its practice as transparent as possible to non-experts. Further revisions of guidance will be undertaken where practicable and appropriate. The CMA has deliberately refrained from consolidating all mergers guidance into a single document because doing so would make updates on specific issues more difficult.

(h) Examples of the factors that would be taken into account to estimate the duration of the SLC are provided at paragraphs 44-45 of the guidance.

(i) A sentence has been inserted at paragraph 8 to clarify that the method for calculating market size is set out at paragraph 36. The CMA will, case by case, gather the best data available from the parties and third party sources. Since the £15 million and £5 million figures are just rough indicators of when the market is of insufficient importance, the decision does not turn on whether the market size is £14,999,999 or £15,000,001.

(j) Footnotes to the CMA's recent practice have been added.

In relation to the counterfactual in Capita/ Vodafone, the CMA undertook a detailed analysis of the parties' submissions in that case. Given the nature of the statutory test for the duty to refer, the CMA does not consider that it is possible or appropriate to apply a different standard to the counterfactual depending on the size of the market affected. The same test must be applied to all cases.

Transactions which are insufficiently far advanced, or insufficiently likely to proceed

Respondent views

2.6 One respondent said it would be helpful if the CMA could confirm whether or not it has used the insufficiently far advanced exception to the duty to refer in any case.

CMA response

2.7 This exception has not yet been used. A footnote has been added to refer to the case team allocation form and to CMA2. This indicates that if the parties cannot demonstrate a good faith intention to proceed after submitting a request for a case team the CMA will simply stand the case team down, with the result that there is no need to publish a decision.

Relevant Customer Benefits

Respondent views

2.8 Respondents made the following comments and suggestions in relation to relevant customer benefits (RCBs):

(a) One respondent preferred the previous guidance (4.4 and 4.5) to the new introduction, for example, because the introduction in the new guidance does not explain why it is not possible to apply an exception to the duty to refer in relation to certain markets, whilst accepting an undertaking in lieu in respect of other markets.

(b) One respondent suggested that there is scope for further clarity in relation to the relationship between RCBs and efficiencies which enhance rivalry, particularly with respect to the stage at which the CMA will take these factors into account. Two other respondents requested examples of specific RCBs (such as those listed in paragraph 7.13 of CMA29: guidance on the review of NHS mergers), with detailed explanations of the evidence and data that the CMA would accept as sufficiently compelling to support the existence of those RCBs.

(c) Two respondents requested that the guidance should set out the description of efficiencies currently contained in paragraphs 5.7.6 - 5.7.18 of the CMA Merger Assessment Guidelines rather than merely giving a cross-reference. They also requested explanation of which of the

efficiencies described in the Merger Assessment Guidelines could be considered as RCBs.

(d) In relation to paragraph 67 one respondent suggested that it should refer to the realistic prospect standard applicable at phase 1. Another respondent suggested inclusion of a statement that a merger might lead to a realistic prospect of a lessening of competition, but the existence of rivalry-enhancing efficiencies may mean this is not substantial.

(e) At paragraph 71 the guidance states that where merging parties expect relevant customer benefits to play a decisive role in the CMA's assessment of a merger, they should collect and present the relevant evidence to the CMA at the earliest possible opportunity. One respondent requested clarification that this should be raised as soon as possible during the pre-notification stage. Another respondent asked whether such evidence could be successfully provided once the phase 1 review period has begun.

(f) Two respondents remarked that the CMA's decisions on NHS Foundation Trust Mergers contained detail which could be incorporated into this guidance.

(g) Three respondents noted footnote 44, which states that in NHS mergers NHS Improvement assisted in verifying the Parties' submissions on benefits, and asked whether the CMA would expect third party verification in all cases. One respondent asked whether the CMA would accept evidence of RCBs other than third party verification.

(h) On respondent asked for examples of the range of periods the CMA would consider reasonable in assessing the timeliness of RCBs.

(i) One respondent requested more detail on the evidence required in assessing the likelihood, timeliness and merger specificity of relevant customer benefits (paragraph 79).

(j) One respondent requested further examples of the types of RCBs that the CMA will typically balance against the loss of competition (paragraph 82).

(k) One respondent suggested that paragraph 84 should refer to the OFT's decision in Global/GCap.

CMA view

2.9 The CMA's response to the points above is as follows:

(a) The relationship between RCBs and undertakings in lieu is now explained in para 86.

(b) While some consideration has been given to the relationship between RCBs and rivalry-enhancing efficiencies in cases such as Asda/Netto (2010) and Global Radio UK/GCap Media (2009) the issue has arisen too rarely to be suitable for generalisation in guidance at this stage. The CMA cannot say in the abstract what evidence and data would be required to accept an RCB and does not feel that it is appropriate to go beyond what it has said in paragraph 74 given that this issue has rarely arisen in phase 1 cases to date.

(c) The CMA prefers to retain the cross-reference to the Merger Assessment Guidelines rather than restating and commenting on that text here because we wish to avoid conflicting texts in the event that either this guidance or the Merger Assessment Guidelines are updated.

(d) Paragraph 67 has been amended to refer to the realistic prospect standard. RCBs are relevant to both phase 1 and phase 2 (hence the open wording of the Merger Assessment Guidelines) but this guidance is about exceptions to the duty to refer, which apply only to phase 1.

The CMA does not generally find it necessary to identify a lessening of competition which is not substantial in its decisions. Should this issue arise, it will be dealt with on the facts of the specific case.

(e) Paragraph 71 has been amended to clarify that RCBs should be raised as soon as possible in pre-notification. While parties may submit new evidence later in proceedings, the earlier it is submitted, the better.

(f) The CMA has published guidance specifically directed at parties involved in mergers of NHS Foundation Trusts. The CMA does not feel that it is appropriate to generalise guidance and decisions given in the NHS context to mergers in general without careful consideration of the facts of specific cases.

(g) The guidance has been amended to clarify that, where relevant, the CMA will consider the views of sector regulators. The position of NHS Improvement is special because it is specifically required to provide advice on patient benefits by section 79(5) of the *Health and Social Care*

Act 2012. Merger parties are welcome to present any relevant evidence on RCBs.

(h) Paragraph 77 has been amended to clarify that the timeliness of RCBs depends on the facts of the case. It is currently not possible to be more specific in the abstract.

(i) The CMA feels that paragraph 79 is as specific as it is able to be at this stage. The NHS mergers referred to in the previous paragraphs provide some examples within the confines of their specific regulatory context.

(j) Paragraph 82 has been amended to emphasise that the weighing of the SLC against the RCB is specific to the facts of each case.

(k) The CMA does not consider Global/GCap a relevant example in paragraph 84 because in that case the efficiencies were rivalry-enhancing.

Appendix A: List of respondents to the consultation on the draft guidance

1. Allen & Overy LLP
2. Ashurst LLP
3. Baker McKenzie
4. Clifford Chance LLP
5. Joint Working Party of the Bars and Law Societies of the United Kingdom on Competition Law
6. The Law Society of Scotland