COMPETITION COMMISSION

Ratcliff Palfinger/Ross & Bonnyman (Commercial Vehicles Tail Lifts Spare Parts Business)

A report on the anticipated acquisition by Ratcliff Palfinger of the commercial vehicles tail lifts spare parts business of Ross & Bonnyman

10 June 2011

Website: www.competition-commission.org.uk

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The Competition Commission has excluded from this published version of the final report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. Some numbers have been replaced by a range. These are shown in square brackets.

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Summary

1. On 18 February 2011 the Office of Fair Trading (OFT) referred the anticipated acquisition of the commercial vehicles tail lifts spare parts business of Ross & Bonnyman Holdings Limited (R&B) by Ratcliff Palfinger Limited (Ratcliff) to the Competition Commission (CC) for investigation and report.

2. Ratcliff manufactures and supplies tail lifts for commercial vehicles and other products, as did R&B until recently. They both still manufacture and supply spare parts to repair and maintain their tail lifts. R&B has run down its commercial vehicles tail lift manufacturing business, with most of its manufacturing rigs scrapped and equipment for production of alternative products installed in their place. It has now stopped manufacturing new tail lifts.

3. On 5 November 2010 Ratcliff and R&B signed an Asset Purchase Agreement (APA) for Ratcliff to acquire the business assets required to supply spare parts for commercial vehicle tail lifts manufactured by R&B (the spare parts business). The APA followed a letter of intent for the purchase signed on 26 July 2010. The most important difference between the two was that the letter of intent included a non-compete clause which provided that R&B would not compete with Ratcliff in the commercial vehicle tail lift manufacture or spare parts markets, and certain other areas of Ratcliff's business, for ten years. In return, Ratcliff would not compete with R&B in certain other areas of R&B's business for three years. These clauses were not included in the APA.

4. We considered whether R&B wound down its tail lift manufacturing business in order to facilitate the sale of its spare parts business, or as a consequence of that sale. We concluded that neither was the case. The tail lift manufacturing business (excluding spare parts) was making low (or negative) margins, we found evidence that the decision to run down and eventually stop manufacturing tail lifts pre-dated the approach to Ratcliff about buying R&B by a year, and we found that R&B has already stopped manufacturing tail lifts whilst the merger has not completed. Further, we found no evidence that Ratcliff had paid more than it thought the spare parts business alone was worth.

5. Given this, and its financial position with the bank, we are satisfied that R&B's rationale for the merger was to sell what had become a non-core business—the tail lifts spare parts business—to realize cash to reduce its debt to the bank.

6. We therefore focused our analysis of the competitive effects of the merger solely on the sale of the spare parts business.

7. We received consistent evidence from the parties to the merger, other manufacturers of tail lifts and their spare parts, and the agents who service and repair tail lifts. All the evidence showed that there is little, if any, competition between tail lift manufacturers in the supply of spare parts. Consequently we did not expect the merger substantially to lessen competition.

8. Therefore we conclude that the merger may not be expected to result in a substantial lessening of competition (SLC).

Findings

1. The reference

1.1 On 18 February 2011 the OFT referred the anticipated acquisition of the commercial vehicles tail lifts spare parts business of R&B by Ratcliff to the CC for investigation and report. The reference was made under section 33(1) of the Enterprise Act 2002 (the Act). The reference requires us to determine:

(a) whether arrangements are in progress which if carried into effect will result in the creation of a relevant merger situation; and

(b) if so, whether the creation of that situation has resulted or may be expected to result in an SLC within any market or markets in the UK for goods or services.[1]

1.2 We are required to publish our final report by 4 August 2011.

1.3 This document, together with the appendices, constitutes our final report. Further information, including a non-commercially-sensitive version of Ratcliff's submission and summaries of evidence from third parties, can be found on our website.[2]

2. The companies

Ratcliff

2.1 Ratcliff is a UK-registered company with headquarters in Welwyn Garden City and a spare parts distribution centre in Leeds. It manufactures and supplies tail lifts for commercial vehicles as well as for passenger vehicles and trains. It also manufactures and supplies spare parts to repair and maintain the tail lifts.

2.2 Palfinger AG (Palfinger) acquired the Ratcliff tail lifts business in 2005. Ratcliff's latest published accounts are for the year ended 31 December 2010. The accounts show that in the year to 31 December 2010 Ratcliff made a loss of £404,000 on a turnover of £11.7 million.

2.3 Palfinger is an Austrian company which operates business in 13 sectors: knuckle-boom loading cranes, container handling systems, forestry and recycling cranes, marine and offshore cranes, tail lifts, railway system solutions, container transfer systems, lifting platforms, bridge inspection equipment, farm cranes, telescopic cranes, as well as attachments and equipment for increasing crane efficiency. The largest product is the truck-mounted knuckle-boom crane. The company is the world market leader in this segment with close to 150 models and a market share of more than 30 per cent. In 2010, Palfinger AG generated operating profits of €34.7 million from revenue of €651.8 million, an operating profit margin of 5.3 per cent. The company has total assets of €677.4 million.[3]

R&B

2.4 R&B is also a UK-registered company. It manufactured and supplied tail lifts for commercial vehicles, and manufactures and supplies ambulance lifts, mezzanine lifts

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[1] Enterprise Act 2002, section 36.
[2] www.competition-commission.org.uk/.
[3] Palfinger AG, Annual Report for year ended 31 December 2010.

and yard lifts. It also manufactures and supplies spare parts to repair and maintain its products. R&B is based in Forfar, Scotland, and is owned and run by the Honig family. Its most recent audited accounts, for the year to 31 December 2009, show that it made a loss of £124,000 on a turnover of £7.8 million.

3. Tail lifts

3.1 Tail lifts are used to transfer goods into and out of a commercial vehicle when the load base of the vehicle is at a different level from that of the loading or unloading point.

3.2 Tail lifts can be segmented by how they are affixed to the commercial vehicle. In the UK, they have traditionally been fitted to the body of the cargo box. These tail lifts work through moving the platform up and down two vertical columns, and are known as column tail lifts.

3.3 The other main type of tail lift is affixed to the vehicle chassis. Chassis-mounted tail lifts were developed for use on mainland Europe; we were told that they had become increasingly popular in the UK over the last 15 years. There are three main types of chassis-mounted tail lift. The cantilever tail lift has a platform which at rest is vertical and can be used as the back door for the vehicle body. The retractable tail lift has a platform which when not in use is underneath the chassis. A motor moves the platform out from under the chassis and back underneath after use. The tuckaway tail lift is similar to the retractable, but the platform is manually positioned under the chassis after use.

3.4 Tail lifts are usually fitted to a new commercial vehicle. The end-user or body builder will normally specify the type of tail lift and order it. Tail lifts typically come with a 12-month warranty; extended warranties are offered. All manufacturers of tail lifts run networks of agents[4] who conduct warranty work, servicing[5] and repairs. The number of agents in a network varies by manufacturer, but most of the larger ones are agents for all the major tail lift manufacturers.

3.5 Tail lift manufacturers also produce spare parts for use in repairs, servicing and warranty work. We were told that most parts for tail lifts were not interchangeable—so, for example, most Ratcliff spare parts could not be used on R&B tail lifts because of differences in design of tail lifts and their constituent parts. Of those parts which are interchangeable, we were told that many, such as switches and some electrical parts, are sufficiently generic that equivalent parts could be purchased in DIY shops. We were told that there was a grey market in spare parts—so-called ‘spurious’ parts—and that imports of copied parts had resulted in the cost of genuine spare parts reducing a few years ago.[6] However, all agents we spoke to told us that they used manufacturer-specific genuine parts where possible when working on tail lifts for several reasons, including concerns regarding liability in the event of accidents caused by failure of parts.

[4] The term agent is used, but there are no written contractual relationships between these companies and the manufacturers; indeed we found few manufacturers with a formal accreditation scheme for its agents.
[5] There are regulations which mandate the regular servicing of tail lifts.
[6] Summary of a hearing with Zepro UK, paragraph 7.

4. The proposed merger and the relevant merger situation

Outline of merger situation

4.1 On 26 July 2010, Ratcliff and R&B signed a letter of intent setting out the basis on which Ratcliff would be prepared to agree an offer for the spare parts business. It set out a transaction value of £[✄] up front, plus £[✄] per month for [✄] (total £[✄]), plus £[✄] for stock. The letter of intent included a provision that R&B would not compete with Ratcliff in the commercial vehicle tail lift manufacture or spare parts markets, or passenger lifts (except ambulance lifts) markets for ten years. In return, Ratcliff would not compete in certain other areas of R&B's business for three years.

4.2 On 5 November 2010, Ratcliff and R&B signed an APA for Ratcliff to acquire the business assets required to supply spare parts for commercial vehicle tail lifts manufactured by R&B (the spare parts business). The APA did not include the proposed non-compete clauses in the letter of intent, but did include a restrictive covenant that seeks to prevent R&B from re-entering the spare parts market for four years.

The rationale for the merger

What the parties and the OFT said

4.3 R&B said that it had decided to exit the tail lift manufacturing market because it had lost significant volume to competitors, and sales of new tail lifts were no longer providing a sufficient contribution to overheads to maintain it as a profitable business. It said that the spare parts business remained profitable and it decided to sell this to reduce its bank debt.[7,8]

4.4 Ratcliff said that it was buying an income stream and this was worthwhile provided the price being paid plus the incremental costs associated with earning that income was less than that income stream (taking account of the time value of money). It said that the incremental costs were limited, given that it already had a similar spare parts business; so, for example, its existing sales staff would also be able to handle sales of R&B spare parts. In its due diligence report to the main board, Ratcliff also highlighted the prospect of being able to achieve sales of an extra [✄] tail lifts of its own design (with subsequent extra spare parts sales on these tail lifts) from customers who would otherwise have purchased products from R&B, although Ratcliff did not include this prospect in its financial appraisal. It recognized that there was a risk it would not achieve these extra sales, but believed that the acquisition paid for itself through spare parts sales alone.

4.5 In referring the case to us for investigation, the OFT said that it did not consider the evidence compelling that R&B would inevitably and imminently exit tail lifts manufacturing absent the transaction. We therefore considered in detail whether the decision to stop manufacturing was taken in order to achieve the sale of the spare parts business.

The rationale for ceasing to manufacture tail lifts

4.6 We focused first on R&B's actions regarding the tail lift manufacturing business.

[7] OFT reference decision, paragraph 106. www.oft.gov.uk/shared_oft/mergers_ea02/2011/Ratcliff.pdf.
[8] The Ratcliff Due Diligence presentation to the Palfinger Main Board said that R&B wanted to exit the tail lift manufacturing business.

4.7 In doing so, we had regard to the situation faced by R&B's shareholders. In particular:

(a) In 2008, both the then main shareholders were looking to retire from the business (which prompted an attempt to sell the whole business—see paragraph 4.13), and more recently the remaining main shareholder has been positioning the business to hand it over to his son.

(b) The company was experiencing severe financial pressures that increased in the period 2007 to 2010.

(c) Tail lift manufacturing was not profitable on a stand-alone basis, and had the lowest margins of all products R&B manufactured.

4.8 We looked first at the financial pressures facing the company. We next examined evidence that the tail lift manufacturing business had been wound down over several years. We then looked at the attempt to sell the whole company and the change of ownership, and finally at the margins for the manufacturing business.

The company was facing financial pressures

4.9 As set out in further detail in Appendix B (paragraphs 3 to 31), the company had a high level of debt—the level of net debt peaked at £3.7 million in 2007, which was already over three times net assets and almost ten times earnings before interest, tax, depreciation, and amortization at that time. Declining margins led to a deterioration of financial ratios. R&B was put under increasing pressure by its bank to reduce its debt and it took actions to sell business assets and release working capital in order to survive. The financial crisis and subsequent recession led to banks restricting lending and the company faced a liquidity shortage.

The tail lift manufacturing business was being wound down

4.10 We saw evidence that R&B had been winding down its activities in tail lift manufacturing over several years:

(a) A company board minute dated 2 April 2008, entitled 'Strategic Review Shareholders Meeting', expressed concern about the performance of the commercial vehicle tail lifts business, commoditization of the product, cut price competition, price pressure and low margins. The document concluded that the best decision was to 'steadily run down the manufacture of tail lifts but continue servicing the spare parts market'.

(b) The Chairman of R&B, Mr Alan Honig, told us that no sales targets had been set for the tail lifts business for the past five years (sales targets had only ever been produced for the purposes of a bonus scheme for salesmen), and that there had been no major tail lift product development since 2006. He said that the company had concentrated on ambulance lifts, yard lifts and mezzanine lifts since 2004.

(c) The trend in unit sales relative to vehicle registrations showed that the company was losing ground in the tail lift market, and the relative decline in unit sales in 2009 was more severe than that experienced by competitors (see Appendix B, paragraphs 34 to 36).

(d) Alan Honig also told us that the number of sales personnel for tail lifts had been allowed to fall from five to zero. Three salesmen retired or resigned before

26 May 2009 and were not replaced. After the transaction was agreed, the final two salesmen retired (in October and December 2010) and were not replaced.

(e) The manufacturing facilities for commercial vehicle tail lifts were rationalized, starting in April 2010. In April 2008, nine assembly rigs were in service in the Roberts Street facility. A further two assembly rigs were located in the Orchardbank facility; this was a rented facility that was closed in March 2010 to save money. The remaining assembly rigs were removed to make space for production of mezzanine and yard lifts. The decision to reconfigure the Roberts Street facility was taken in late 2009, when new lifting equipment was ordered. This installation of the lifting equipment, into the area previously used for tail lift manufacture, was completed in April 2010.

(f) Subsequently, on 6 January 2011 the company removed and scrapped four assembly rigs and installed a paint facility on the site. At the time of the reference of the merger to us, R&B had only two tail lift manufacturing rigs, and these were being used to complete the existing order book before being scrapped to make space for a powder coating facility—we were told by Alan Honig that R&B had stopped taking new orders around Christmas 2010. R&B had already effectively committed itself to stopping manufacturing tail lifts, even though the merger had not been completed.

4.11 At the same time, R&B has invested in equipment needed for its mezzanine and ambulance lifts businesses, including the lifting equipment referred to in paragraph 4.10*(e)*, and spray painting and powder coating facilities.

4.12 In light of the company's ownership, management and size, we would not expect to find more comprehensive documentation of strategic decisions to exit the business than has already been supplied to the OFT and ourselves. The evidence that is available suggests that the decision to stop manufacturing tail lifts was originally made in April 2008—over a year before Ratcliff was first approached about buying any part of R&B; that actions were taken on this decision independently of the sale of the spare parts business; and that R&B has exited the manufacturing market notwithstanding that the merger of the spare parts business has not yet been completed.

The attempt to sell the whole company and the change of ownership

4.13 In 2008, the owner of R&B engaged Catalyst, an adviser in divestments, to try to sell the entire company. Catalyst approached a large number of potential purchasers, including many of R&B's competitors. It first approached Ratcliff's parent company Palfinger in May 2009. In December 2009, Catalyst reported that it was unable to find a buyer for the company at a price which would make sense to the R&B shareholders given the level of debt in the business, and that it had only found one buyer—Ratcliff—interested in any part of the business (the tail lifts spare parts business).[9]

4.14 On 23 December 2009, the Honig family purchased the 50 per cent of the shares that it did not already own, so that the then co-owner, Mr Freddie Craig, could retire from the company. The price agreed for these shares was £[✂]. Alan Honig became Chairman of the company and his son Mr Marcus Honig became Managing Director.

[9] R&B separately negotiated the sale of its shutter door business in December 2009.

4.15 The combination of debt and equity resulted in an enterprise value of the company of approximately £2.5 million at the transaction date. The gearing was [✂] per cent.[10] Alan Honig told us that the value of the company's shares was [✂], and that Freddie Craig was intending to end his involvement with the company for personal reasons. The price was agreed between the shareholders and enabled Freddie Craig to end his involvement in the business. In our view, the change of ownership and management in December 2009 and the longer-term plans of Alan Honig to retire over a period of time as his son Marcus Honig took on increasing responsibility and ultimate leadership of the company was in line with a change in the strategic direction of the company to focus on more profitable products. Implementation of the succession plan commenced before the proposed transaction with Ratcliff was agreed.

Margins for the manufacturing business were too low

4.16 Alan Honig told us that commercial vehicle tail lift prices had fallen in recent years to a level that made it no longer viable for the company to continue production because for many products the price was less than the combined cost of materials, painting and shipping.

4.17 The company has reduced its manufacturing facilities from three to two premises (Roberts Street and Market Street, following the closure of Orchardbank) in a process that started in 2008. R&B is still making changes to its remaining facilities to optimize the infrastructure and layout for the products it intends to manufacture going forward. The company has limited access to capital for investment in manufacturing facilities, particularly in light of the issues it faces with respect to bank debt (see Appendix B, paragraphs 20 to 31). Within these constraints, the company's management uses the mark-up on materials costs for individual products to make decisions about which products to produce.

4.18 We examined the mark-up on materials costs and the product margin for the company's products using management accounting information for 2009 and 2010. The analysis is set out in Appendix B, paragraphs 37 to 51. This showed that:

- the mark-up on materials costs for the three tail lift products ('retractables', 'column lifts' and 'tuckaways') was lower than for access lifts and moving decks; and

- the product margin for the three tail lifts products was lower than for access lifts and moving decks and was negative in 2009 and 2010 for column lifts (the main product, accounting for 85 per cent of tail lift sales in 2010) and tuckaways.

4.19 We note that the overhead allocation methodology does not attribute overheads to spare parts because there is no reliable estimate for standard production hours. We explored whether, when taken together with the spare parts business, there was the same incentive to close tail lifts. We therefore produced our own estimate for the 'blended margins' of the commercial vehicle tail lifts business (ie including finished goods and spare parts), based on a number of alternative assumptions to absorb overheads within the combined sales of spare parts and finished goods. We set out our methodology in Appendix B, paragraphs 50 and 51. This shows that in 2010 the blended 'mark-up on materials costs' was in line with that of the company, at [✂] per

[10] Gearing = debt / (equity + debt). Assumptions: £[✂] net debt on the company's balance sheet at 31/12/2009 plus £[✂] equity.

cent. In the same year the blended product margin was [✂] per cent, which was higher than at least one continuing product line.[11]

4.20 On first inspection, this suggested to us that it might be profitable for R&B to remain in the commercial vehicle tail lifts market. Customers may consider their tail lift purchase on the basis of lifetime value, which includes the ability to service and maintain the lifts (ie consume spare parts); and suppliers may benefit from higher margins on spare parts that offset the lower margins on the tail lifts. If sales of new products ceased, the profit stream from spare parts would be rapidly eroded by the obsolescence of the installed base, reducing the value of the spare parts business.

4.21 Alan Honig told us, however, that he did not consider the 'blended margin' to be relevant to his decisions; because the company had limited production capacity and floor space, the profit-maximizing strategy was for the company to focus manufacturing on the products with the highest mark-up on materials and/or the highest contribution. He said that he had long experience of the cost of materials and hours needed to make his products and he required little additional information from overhead-allocation techniques to make decisions.

4.22 Alan Honig also told us that a new tail lift would not generate a positive contribution from spare parts for at least one year, because the first year was covered by a warranty, for which the company was liable. He said that spare parts generally only generated a positive contribution in the period after the expiry of the warranty, until the end of the lift's useful life.

4.23 Our analysis confirmed the company's conclusion that margins in the tail lift manufacturing business (excluding spare parts) were low or negative, and unsustainable in the long run unless costs could be reduced significantly. We noted that if R&B had looked at the product margins of its tail lift manufacturing and spare parts business on a blended basis, it would have been positive, and higher than the product margins for some of its other products (though these product margins did not take account of spares for those products). We believed that R&B did not look at its tail lift business on a blended basis and that it was reasonable for it not to do so. As explained above in paragraph 4.9, the assessment of capital structure and access to capital showed that the company was under financial pressure and faced restrictions on its productive capacity. A separate analysis in Appendix B (paragraphs 52 to 55) showed that the company had limited capacity to make major reductions in its cost base. Our analysis also confirmed that the profitability of other products was higher (see Appendix B, paragraphs 37 to 49).

4.24 We were satisfied that the company was restricted in what it could produce because of its limited access to capital, and that it was reasonable in those circumstances for it to focus on what it believed to be higher-margin products.

4.25 Alan Honig also told us that having decided to cease production of tail lifts, he had embarked on a reconfiguration of his facilities and had made investments (eg in overhead lifting cranes) to produce higher-margin products. He said that the factory floor area currently occupied by stores of spare parts would be more productively used by relocating the equipment within the company's two sites so that precision machinery used to produce components could be placed away from the welding and assembly activities.

[11] Note that there may be some activities from cantilever lifts included in the access lifts contribution.

4.26 We visited R&B's facilities. The company is now concentrating on low-volume products that require specialist design work to tailor the product to specific needs and on which it is able to achieve higher margins. This makes use of the company's expertise in product design and engineering of hydraulic and electro-mechanical systems and the skills of its workforce to manufacture products to a high quality. The company lacks the scale and resources to mass-produce using automated assembly lines. On this basis, it is our view that it is unlikely that the company could significantly increase production. This is in line with the evidence that R&B is following a strategy of moving away from a commoditized product, tail lifts, towards lower-volume higher-value products.

4.27 The financial analysis shows that the evidence of the company's winding down of its tail lift manufacturing business is in line with the reality of that business's viability. We conclude that it was reasonable for R&B to make a decision to stop production of commercial vehicle tail lifts and concentrate on higher-margin products—indeed the decision was based on sound commercial logic—and it was rational for the company to consider separately how best to crystallize the value remaining in spare parts.

The rationale for buying the tail lifts business

4.28 In paragraph 4.4, we set out Ratcliff's stated rationale for the merger. We looked at evidence related to Ratcliff's rationale.

4.29 We considered first whether there was any evidence of Ratcliff paying more than it thought the spare parts business alone was worth. This might indicate that Ratcliff had paid R&B to stop manufacturing tail lifts. In our view, there is no evidence that Ratcliff paid a strategic premium for the exit from the manufacturing business. Our analysis is set out in Appendix B, paragraphs 57 to 65. We found that:

(a) The primary valuation methodology used by Ratcliff to value the business was a discounted cash flow based on a forecast cash flow from the spare parts business under two scenarios (realistic and pessimistic cases), and that the forecasts did not include any cash flow relating to the sale of new tail lifts in either scenario. Ratcliff told us that it made the acquisition decision based on the pessimistic case and that this represented conservative assumptions about the likely performance of the business.

(b) Ratcliff applied two discount rates within the range 5 to 20 per cent to evaluate acquisitions, based on standard corporate assumptions required by its parent company. Based on the lower discount rate, [✂] per cent (the hurdle rate), the fair market value of the spare parts business was higher than the consideration paid. Based on the higher discount rate, [✂] per cent (the target rate), the fair market value was less than the consideration. Given this, as a cross-check, we examined the internal rate of return (IRR) on the forecast cash flows, and found these to be between 10 and 20 per cent in both cases. We concluded that the IRR represented a reasonable expected return in both cases. Bearing in mind that the pessimistic case contained more conservative (hence lower-risk) assumptions, we would expect it to correspond with a lower IRR than the realistic case. In summary, we found that there was no evidence of a strategic premium within the valuation.

(c) We also compared the proposed consideration with the valuation of the business at the end of 2009 (based on the price the Honig family paid Freddie Craig for his shares—see paragraph 4.14). Whilst the proposed consideration is around the same as the enterprise value of the company in December 2009, we concluded that it was not reasonable to make a direct comparison between the two trans-

actions. We noted that circumstances were different with respect to the timing, motivation (eg factors personal to the selling shareholder) and perceived negotiating positions of the parties involved. Moreover, there had been a substantial recovery in the stock market during this period. Between 31 December 2009 and 31 December 2010, the FTSE All-Share Index increased by 11 per cent and the AIM Index increased 43 per cent and the Palfinger share price increased by 85 per cent.

4.30 Ratcliff told us that the R&B spare parts business could be absorbed by Ratcliff's national parts centre and distribution network with little, if any, additional cost, and that the resulting scale benefits could mean that the spare parts business was worth more to Ratcliff than to R&B.

4.31 Having found no evidence of Ratcliff paying R&B more than it thought the business was worth, we also considered whether it could have acquired the business for nothing (and thus by buying it was paying R&B a strategic premium). Ratcliff told us that it had been aware for some time that R&B was financially stretched, to the point where it thought that its exit from the tail lift market was inevitable.

4.32 Ratcliff explained that a relevant consideration in acquiring the spare parts business from R&B via an asset purchase agreement (as opposed to out of administration, in the event that R&B collapsed) was that Ratcliff could be certain about what assets it was acquiring. In addition, the survival of R&B post-deal would preserve the supply chain of spare parts (including those to be manufactured by R&B on a contract basis in future) and the availability of ongoing technical advice about historical sales. It also said that when another tail lift manufacturer, the Ray Smith Group, collapsed, there had been what it described as a fire sale, and it had not been able to acquire any assets in which it might have been interested. Ratcliff thought it was by no means certain that if it had left R&B to go into administration it would have been successful in acquiring the spare parts business.

Conclusion on rationale for ceasing manufacture of tail lifts

4.33 We found that there were good reasons for R&B stopping manufacturing tail lifts. R&B was under pressure to reduce its bank debt. The tail lift business (excluding spare parts) was making low (or negative) margins and R&B's facilities were not well suited to modernizing the process for mass production of tail lifts. R&B's owners decided instead to focus on higher-value lower-volume business. We found that the initial decision to stop manufacturing, and some of the subsequent actions, in particular not replacing departing sales staff, pre-dated the decision to sell the spare parts business, and R&B had stopped manufacturing tail lifts before the merger had completed.

4.34 We considered whether, despite it not appearing in the APA, the ten-year non-compete clause in manufacturing offered by R&B (see paragraph 4.1) was implicit in the agreement to sell the business. We found no evidence that it was; when we asked Ratcliff in an oral hearing, it told us that there was no implicit understanding to that effect.

4.35 The evidence also showed that the exit from tail lift manufacturing was not to facilitate the spare parts merger, nor was it a consequence of the merger. There was no evidence that Ratcliff had paid more than it thought represented a fair price for the spare parts business (see paragraph 4.29). Also, as set out above, we were satisfied that R&B's decision to run down the tail lift business pre-dated the decision to sell the spare parts business to Ratcliff, and the exit was completed before the merger.

4.36 We conclude, therefore, that R&B's decision to stop manufacturing tail lifts was neither to facilitate the sale of the spare parts business nor a consequence of the merger.

Rationale for selling the spare parts business

4.37 Having decided that it wanted to stop manufacturing tail lifts, R&B needed to decide what to do with the spare parts business. Simply stopping manufacture of spare parts would have left customers without spare parts and faced with the prospect of having to replace tail lifts with several years of useful life left in them simply because of the difficulty of sourcing spare parts. Such a scenario could have been damaging for R&B's reputation.

4.38 The more likely options for the spare parts business were that R&B continued manufacturing and selling spare parts, or it sold the spare parts business.

4.39 As noted in paragraphs 4.7*(b)* and 4.9, the company had a high level of debt, with £3.7 million net debt in 2007. R&B experienced deteriorating financial performance and financial risk increasing between 2009 and 2010. The company's auditors added an 'emphasis of matter' in relation to going concern questions in the 2009 statutory accounts. R&B's bankers had applied pressure on the company to reduce debt at least as far back as 2008. The majority of R&B's debt was in the form of term loans that were originally due for repayment in [✂].

4.40 The company's access to bank debt was sharply reduced in 2009/10, and it was unable to extend the maturity of debt or restructure its borrowings (eg through new loans). The company supplied details of the increasing pressure it was facing from its bank to repay term loans that matured at [✂]. The invoice financing facility was also reduced. The change in bank policy and its willingness to lend may be due to a combination of factors, including the financial market conditions during the period and risk assessment of the company based on its borrowings and prospects.

4.41 Given that bank finance was not available, the company and its shareholders sought alternative sources of financing and took a number of actions, including the sale of the Shutter Doors business in December 2009, raising £0.5 million cash, the injection of £[✂] as a director's loan in 2010, and the sale of stock to Ratcliff for £[✂].

4.42 The sale to Ratcliff of some of R&B's stock of spare parts took place in December 2010, raising £[✂]. If the merger does not proceed, the terms of the sale mean that the stock will be returned to R&B and R&B will need to repay Ratcliff.

4.43 Against this background, we conclude that the reason R&B sold the spare parts business, rather than continued to operate it, was to realize cash in order to reduce its bank debt.

Conclusions on the rationale for the proposed merger

4.44 The proposed merger was the sale of the R&B spare parts business to Ratcliff. We found that R&B made a decision in the normal course of business to run down and stop its tail lifts manufacturing business, and to focus on higher-value lower-volume products. As a consequence, the associated spare parts business would have a limited lifespan. Given this, and its financial position with the bank, we are satisfied that the rationale for the merger was to sell what was becoming a non-core business —the tail lift spare parts business—to realize cash to reduce its debt to the bank.

4.45 We conclude that the decision to stop manufacturing and selling tail lifts was not made in order to facilitate the sale of the spare parts business, nor was it a consequence of the merger. Given this, we do not consider tail lift manufacturing further.

Jurisdiction

4.46 Under section 36 of the Act, and pursuant to our terms of reference (see Appendix A), we are required to decide whether a relevant merger situation will be created.

4.47 Section 23 of the Act provides that a relevant merger situation is created if two or more enterprises have ceased to be distinct within the statutory period for reference and either the share of supply test or the turnover test specified in the Act is satisfied.

4.48 We are satisfied that the spare parts business of R&B is an enterprise for the purposes of the Act, and that it will cease to be distinct as a result of the transaction described in paragraph 4.2.

4.49 Under section 23 of the Act, the share of supply test is met if, as a result of the merger, the enterprises which ceased to be distinct have a share of supply of goods or services of any description in the UK, or in a substantial part of the UK of at least one-quarter, or if it already supplied at least one-quarter, it must have increased its share as a result of the merger.[12]

4.50 Ratcliff and R&B are both active in the manufacture and sale of spare parts for column tail lifts. The parties, and third parties to whom we spoke, told us that most spare parts were not interchangeable (see paragraph 3.5), and on that basis we assume that the share of supply of column tail lifts sold is a good proxy for the share of supply of column tail lift spare parts sold. The parties accepted this argument.

4.51 In 2010, Ratcliff sold [✂] column tail lifts and R&B sold [✂].This gave Ratcliff a market share of [30–40] per cent and R&B a market share of [10–20] per cent. Assuming that the share of supply of tail lifts is a good proxy for the share of supply of spare parts, we find that the merger satisfies the share of supply test.

4.52 We therefore conclude that if the proposed transaction is carried into effect, a relevant merger situation under section 23 of the Act will be created.

5. The competitive effects of the proposed merger

5.1 The parties are both active in supplying spare parts for commercial tail lifts. The transaction brings together these two businesses and we considered whether customers would face a loss of competition as a result through the reduction in the number of suppliers and the loss of rivalry allowing Ratcliff to exercise market power unilaterally, by increasing prices or reducing the quality of service to all or some commercial vehicles spare parts tail lift customers.

5.2 In assessing the effect of the transaction on competition in this market, we paid particular attention to segmentation between the different manufacturers of commercial tail lifts, and in particular whether spare parts supplied by Ratcliff are used only for Ratcliff commercial tail lifts, whilst those supplied by R&B are used only for R&B commercial tail lifts.

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[12] The application of the share of supply test is different from the identification of economic markets undertaken as part of any analysis of competition within an economic market. See *Merger assessment guidelines, CC2 (revised)*, September 2010 (the Guidelines), section 3.3.

5.3 We have not found it necessary to consider segmentation between different types of spare parts as we received no evidence suggesting that the effects of the merger might be markedly different for particular types of parts. In effect, we have looked at the effects of the merger in a market comprising all spare parts for tail lifts.

Counterfactual

5.4 We considered what was likely to have happened in the absence of the merger (the counterfactual).[13]

5.5 For the reasons set out in Section 4, we find that, without the merger, R&B would still have stopped manufacturing tail lifts.

5.6 With respect to the tail lifts spare parts business, without Ratcliff as a buyer for the spare parts business, R&B's options were to retain the business, sell it to another party (though we are not aware of other potential bidders) or shut down the spare parts business (which seemed unlikely to us given that it is profitable and given the possible negative impact on reputation of such a course of action).

5.7 Given that we find in paragraph 5.27 that there is little if any competition between manufacturers of spare parts, our conclusions on the merger are the same whatever R&B would do with the spare parts business in the counterfactual, and we do not need to reach a view on the most likely counterfactual for the spare parts business.

Competition between providers of spare parts

5.8 We considered the degree of competition between suppliers of spare parts for tail lifts.

Evidence from Ratcliff and R&B

5.9 Ratcliff submitted that, given the lack of substitutability between spare parts, there was no competition in relation to spare parts for tail lifts produced by each manufacturer. Put another way, Ratcliff considered that there were separate economic product markets in relation to spare parts for the tail lifts of each manufacturer.

5.10 Ratcliff and R&B submitted that both parties presently had 100 per cent or close to 100 per cent of the market for the supply of spare parts for their tail lifts. Ratcliff said that it did not supply spare parts used in R&B tail lifts; similarly, R&B said that it did not supply spare parts used in Ratcliff tail lifts.

5.11 As part of the due diligence process, Ratcliff analysed R&B spare parts sales and estimated that around [✂] per cent of spare parts were generic. These included fixings, electrical parts and hydraulics/hoses. The other [✂] per cent of parts were bespoke to the manufacturer. Some of these bespoke parts would be covered by intellectual property, but the majority are capable of being manufactured by another supplier. However, it is unlikely to be cost effective for a manufacturer to produce spare parts for tail lifts manufactured by another manufacturer (referred to in the industry as 'spurious' parts), given the small number of parts involved (the manufacturer is producing those parts for both new tail lifts and spare parts) and the disadvantage that 'spurious' parts will always have against original parts.

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[13] The Guidelines, paragraph 4.3.1, state: 'The application of the SLC test involves a comparison of the prospects for competition with the merger against the competitive situation without the merger. The latter is called the "counterfactual".'

5.12 Ratcliff said that there was currently no direct competition in relation to the vast majority of spare parts for tail lifts produced by each manufacturer. However, manufacturers were constrained by the whole-life cost of the tail lift.

5.13 R&B provided us with minutes of a board meeting held on 2 April 2008 which said that many parts could not be replicated by other suppliers: 'The sale of tail lift spare parts had shown interesting profitability assisted by the fact that many of the R&B parts were purpose designed and built, and could not be replicated by spurious suppliers.'

5.14 The sale document prepared by Catalyst said:

> It should be noted that the spare parts sales with [✂] margins are protected because of unique design of the components and also the fact that many of these products are cast and extruded, and so cannot be copied without considerable cost of moulds and dies which are in the company's ownership.

Evidence from other manufacturers

5.15 Anteo UK Ltd (Anteo UK)[14] told us that there was no requirement for Anteo UK's agents to use the manufacturer's spare parts, but most of its spare parts were specific to the Anteo product, and therefore it supplied all the Anteo parts in the UK. Anteo UK said that 90 per cent of its parts were bespoke to the Anteo tail lifts. Anteo UK thought that there was some interchangeability on parts between Ratcliff and R&B on items such as power packs. However, it did not think there was a lot of competition in the spare parts market. If a customer had an Anteo product, he rang Anteo UK; if he had a Dhollandia UK Ltd (Dhollandia) product, he rang Dhollandia (either through the agent or the manufacturer).

5.16 Del Equipment (UK) Limited (Del Equipment) told us that there was an unofficial requirement for agents to sell genuine spare parts and Del Equipment believed it was the safer option for its agents, since they would not want to risk upsetting Del Equipment. In any case, another company's parts were unlikely to fit Del Equipment products; it thought that about 99 per cent of its spare parts were unique to its tail lifts. Del Equipment thought that the only parts that would fit both Ratcliff and R&B tail lifts were likely to be power packs.

5.17 Dhollandia told us that on repair work carried out on its behalf and on repair works on its products it would expect agents to use genuine parts. Dhollandia thought that there was some use of spare parts from one manufacturer being used on another manufacturer's tail lift, though it did not think this was the norm. It thought that some items, such as power packs, could be interchangeable between manufacturers; others, such as runners, were unlikely to be substitutable. Dhollandia did not encourage anybody to buy Dhollandia spare parts for use on other makes of tail lift.

5.18 Zepro UK Ltd[15] told us that it required its agents to use the manufacturer's genuine spare parts because of a 12-month warranty guarantee, but after that agents were free to do as they wished.

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[14] Summary of a hearing with Anteo UK, paragraphs 6 & 7.
[15] Summary of a hearing with Zepro UK, paragraph 7.

Evidence from agents

5.19 The degree of competition between R&B and Ratcliff prior to the merger is contingent on the manufacturers' agent agreement, the proportion of spare parts that are bespoke to the manufacturer and degree to which one can interchange R&B and Ratcliff spare parts. The proportion of generic parts that can be sourced elsewhere is not of primary concern because we are seeking to establish the extent to which R&B and Ratcliff constrained each other before the merger.

5.20 R&B and Ratcliff primarily sell spare parts to accredited agents (see paragraph 3.4). Agents supply spare parts for multiple manufacturers. Ratcliff said that nearly all its sales were through agents.

5.21 Both parties use networks of agents. Ratcliff operates an accreditation scheme that has a clause requiring repairers to use only genuine parts to maintain accreditation and an agreed discount: [✄].

5.22 The scheme also involves periodic audits of the agents' parts stock. Three agents we spoke to told us that Ratcliff enforced this clause. One agent said that Ratcliff could carry out spot checks on repairs to ensure that genuine parts had been used in addition to its periodic audits.

5.23 R&B does not have a standard contract for agents; however, third parties told us that there was an understanding that only genuine parts should be used. One agent told us that whilst it only used genuine parts for R&B tail lifts, R&B had not enforced the genuine parts requirement for a while. It said that, previously, R&B had analysed key component purchases; R&B would look at the top 20 or 40 products and cross-check with agent invoices to ensure usage. It would ask where the agent had sourced products from if sales of key items appeared low.

5.24 There was a consistent response that agents use genuine parts where possible. Responses are summarized in Table 1. All agents estimated that they sourced approximately 90 to 100 per cent from the relevant manufacturer.

TABLE 1 **Summary of responses from agents**

Agent	*Manufacturer sourced %*	*Reasons for sourcing from the manufacturer*
Alfa Tail Lifts Ltd	95	Parts were usually pertinent to that specific lift, warranty work might/would not be authorized if 'spurious' parts were purchased and used.
Dependable bodies	~100	Part of agents' agreement. Believed manufacturers did check that using genuine parts. Little compatibility between the R&B and Ratcliff parts as bespoke to manufacturer.
Double 4 Ltd	90	Agency requirement.
Hills Body works	90	Needed to use genuine parts as part of agency agreement. Manufacturers did annual audits. Ratcliff also did spot checks—it checked a repair job to make sure genuine parts. If you failed you were removed from agency accreditation scheme.
Humberside Tail Lifts	~100	Only used genuine parts. Part of accreditation scheme, company philosophy. A lot of R&B and Ratcliff parts were not interchangeable. Got the odd part when it was an electrical part. The percentage of parts which were interchangeable between Ratcliff and R&B was probably less than 1 per cent.
Hydraulic mobile services	~100	Specialized product. Better quality, some parts could not source from elsewhere. Some compatibility between R&B and Ratcliff spare parts but not much. Still specialized. Sometimes used rival manufacturer's part but this was due to availability rather than price. Suspected not a great difference in price.
Johnston Engineering (Falkirk) Ltd	Vast majority	Not 100%, but the amount it did not buy from the specific manufacturer was marginal. The opportunity to do so was relatively small because the interchangeability of parts was relatively small due to the manufacturers' specification being largely bespoke. Additionally the manufacturers did not like the use of 'spurious' parts as they compromised any warranty issues and ultimately might lead to the end of an agency agreement. For the purposes of our investigation, its purchase of such parts was negligible. Quality and reliability were paramount.
Lifting & Cooling	100	Customer preference, OEM quality, warranty.
Marshall Web	90	Preference for genuine spare parts. View of company rather than agency agreement. Also warranty issues. Some parts were universal and one could sometimes interchange parts between manufacturers. Interchanging parts based on industry knowledge rather than advertisement from manufacturer. Would interchange due to availability rather than price, ie if truck stuck at side of the road would repair.
Pullman Fleet Services	90	Quality, price, availability.
Ransome Engineering	90	Sourced from manufacturer as this had always been company policy and the preferred option. Warranty issues, company preference. One could not really interchange between R&B and Ratcliff as parts were different.
Saltash DAF Limited	100	As an agent, manufacturer loyalty.
Stewarts Tail lifts	90–95	As an agent, it was required and for the warranty supplied. Many parts were only available from the manufacturer.
Stone Hardy Limited	90–95	It was the only place to get the majority of parts. Needed to buy from manufacturers *(a)* bespoke to lift and *(b)* part of the agency agreement. • Enforcement of agency agreement. • Ratcliff had a service team that conducted audits. Should be annually but not always the case. Ratcliff would ask where the parts sourced and check the parts department. • R&B had not enforced for a number of years but previously looked at key competent purchases. It would look at top 20/40 products—cross-check with agent's invoices and ask where sourced products from. • One could not interchange between R&B and Ratcliff. There were some parts that could be used on both but manufacturers managed to keep parts bespoke.

Source: CC discussions with agents.

5.25 Several agents also told us that the majority of spare parts were bespoke to the manufacturer. Humberside Tail Lifts estimated that less than 1 per cent of parts were interchangeable between Ratcliff and R&B whilst other third parties said that some could be substituted. Parts that were interchangeable tended to be parts outsourced from R&B and Ratcliff to third parties, such as electrical items or simple generic items like rubber hoses. Some agents said that there were instances where an R&B part might be fitted on a Ratcliff lift and vice versa, but this was due to availability and need (ie if the part was on the service van) rather than competition and price.

The extent of competition on spare parts

5.26 The evidence we received showed a consistent picture. Manufacturers of tail lifts design their own products and most of the parts they use are designed and manufactured for that tail lift—and are not interchangeable with parts used in tail lifts designed by other manufacturers. A small percentage of parts are interchangeable, but these tend to be generic items (such as power packs), some of which can be sourced from multiple outlets, not just from tail lift manufacturers. Agents will nearly always use spare parts sourced from the tail lift manufacturer that made the tail lift they are working on, because of the limited ability to fit parts made by other tail lift manufacturers, concerns about liability should a generic piece fail, and because of either explicit or implicit requirements of the manufacturers to use only genuine spare parts in repairs. Whilst we were told of a grey market of 'spurious' parts, we did not receive any evidence to suggest that manufacturers encouraged agents or anyone else to use their spare parts on other manufacturers' tail lifts.

5.27 Overall, we found that there is little, if any, competition between tail lift manufacturers in the supply of spare parts.

5.28 Consequently we did not expect the merger substantially to lessen competition.

Conclusions on the SLC test

5.29 We conclude that the merger may not be expected to result in an SLC.