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## **Anticipated acquisition by HMV of 15 Zavvi stores**

ME/4036/09

The OFT's decision on reference under section 22(1) given on 28 April 2009  
Full text of decision published 14 May 2009

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**Please note that square brackets indicate figures or text which have been deleted or replaced at the request of the parties for reasons of commercial confidentiality**

### **PARTIES**

1. **HMV Group plc (HMV)** is active in selling entertainment products. It retails pre-recorded music, films, electronic games and peripherals, MP3 players and a small range of books (mainly music/artist related) under the HMV and FOPP brands. There are approximately 237 HMV branded and eight FOPP branded retail outlets in the UK. HMV retails books under the Waterstone's brand from approximately 309 stores in the UK. HMV also operates websites in the UK and the Channel Islands retailing music, games, films and books.
2. **Zavvi Retail Limited (Zavvi)** was also active in the sale of a broadly similar range of entertainment products to those sold by HMV as described above. Zavvi entered into administration on 24 December 2008.

### **BACKGROUND**

3. Zavvi traded from 114 stores across the UK and Ireland. It was created through a management buy out (MBO) of the Virgin Megastore division of the Virgin Group in September 2007.
4. Zavvi (and its predecessor, Virgin Megastore) traded at a loss for a number of years. Its business was highly seasonal, with peak demand occurring across November and December. However, it experienced considerable

cash flow difficulties when EUK (a subsidiary of Woolworth plc), the sole supplier of stock to Zavvi, went into administration on 27 November 2008. As a result, Zavvi was not able to source stock in its usual way and faced difficulty obtaining stock at acceptable prices or on favourable credit terms. The administrator of Zavvi, Ernst & Young, told the OFT that this placed considerable pressure on Zavvi's working capital and with quarterly rent payments due of £13 million on 25 December 2008, the directors of Zavvi considered that they were unable to be able to meet these or other creditor liabilities as they fell due.<sup>1</sup>

5. Given this backdrop, on 12 December Ernst & Young were employed to attempt to carry out an emergency restructuring of the business. This did not prove possible and Zavvi went into administration on 24 December 2008.<sup>2</sup>
6. The administrator informed the OFT that the prospect of rescuing the company as a going concern was not viable by the time Zavvi went into administration. The administrator confirmed that Zavvi's significant operating losses made it unlikely that equity investment could be secured, and that, following the failure of EUK, it was difficult for Zavvi to be able to secure stable and competitive supplies. The main purpose of the administration, after failure to rescue the whole of Zavvi as a going concern, was therefore to continue to trade as many stores as possible with a view to achieving a going concern sale of as many of them as possible.
7. It is against this background that HMV acquired 15 of the former Zavvi stores. To date, the only other entity that has acquired any stores is Head Entertainment LLP (Head), a newly incorporated company run by the former management of Zavvi (discussed further below).<sup>3</sup>

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<sup>1</sup> Discussions between Ernst & Young and OFT.

<sup>2</sup> Ernst & Young document dated 13 February 2009, Administrators Statement of Proposals pursuant to paragraph 49 of schedule B1 to the Insolvency Act 1986. The purpose of the administrator was stated to be threefold: 'to rescue the company as a going concern; to achieve a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration); to realise property in order to make a distribution to one or more secured or preferential creditors'.

<sup>3</sup> A limited liability partnership incorporated on 2 February 2009 by former Zavvi chief executive Simon Douglas and business partner Les Whitfield.

## TRANSACTION

8. HMV has taken over 15 stores that were previously trading as Zavvi prior to its entry into administration in the following three tranches:
  - (i) nine stores on 14 January 2009<sup>4</sup>
  - (ii) five stores on 16 February 2009,<sup>5</sup> and
  - (iii) one store located in the Manchester Arndale Centre (Manchester Arndale) on 26 March 2009.
9. Collectively these 15 stores are referred to in this decision as the 'Acquired Stores'. The OFT understands that the Acquired Stores have been initially occupied under licence by HMV until legal completion in the form of transfer of leasehold interests (or grant of a new lease) can occur. This cannot take place until formal landlord consents to assign have been executed (or a new lease has been granted). Transfers of leasehold interests have been executed for only some of the stores, and therefore, as a whole, the transaction still remains anticipated.<sup>6</sup>
10. This investigation was instigated by an OFT own-initiative enquiry and the original un-extended administrative deadline for its consideration was 14 April 2009. In line with section 27(5) of the Enterprise Act 2002 (the Act),<sup>7</sup> the timetable for consideration of this transaction re-commenced at the point at which the OFT received a satisfactory submission in relation to each additional tranche of purchases. The OFT was notified of HMV's final acquisition of the Manchester Arndale store on 9 April, and as a consequence the revised administrative deadline is 10 June 2009.

## JURISDICTION

11. A relevant merger situation arises when two or more enterprises cease to be distinct and either the UK turnover test or the share of supply test set out in section 23 of the Act is met.

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<sup>4</sup> Peterborough, Plymouth, Southend, Glasgow Silverburn, Glasgow Fort, Bournemouth Castlepoint, Salisbury, Crewe, Teeside.

<sup>5</sup> Glasgow Buchanan Galleries, Croydon, Nottingham, Fulham and Hastings.

<sup>6</sup> Since the OFT's decision was made we understand that the transfers of the leases in respect of the Bournemouth and Fulham stores have been executed.

<sup>7</sup> The application of section 27(5) of the Act in this case is discussed in more detail further below.

12. In relation to anticipated mergers, the requisite test for the OFT is that it has to reach a belief that it is or may be the case that arrangements are in progress or contemplation which, if carried into effect, will result in the creation of a relevant merger situation (section 33(1) of the Act).
13. The turnover generated by the Acquired Stores between December 2007 and November 2008 was approximately £[ ] million; the turnover test was therefore not met. However, HMV and the Acquired Stores overlap in the bricks and mortar supply of home entertainment products, and in particular recorded music, films and games and accessories and the share of supply test in section 23 of the Act is met in relation to the bricks and mortar retail of recorded music and DVDs in which HMV and the acquired stores hold [ ] per cent.
14. The OFT has considered carefully in this case whether it is or may be the case that enterprises would cease to be distinct under the arrangements in question. Specifically, the OFT considered whether:
  - (i) the Acquired Stores taken over by HMV should be considered to be 'enterprises' for the purposes of the Act, and
  - (ii) they should collectively be aggregated together under section 27(5) of the Act and treated as a single relevant merger situation.

#### **Enterprises ceasing to be distinct**

15. According to the administrator, the most valuable Zavvi assets were the leases of its properties. Although the administrator took primary charge of the sale of the Zavvi assets, any prospective assignment of leases (or granting of new leases) had to be negotiated through the relevant landlord of each of the stores. The administrator had the ability to place a prospective lessee temporarily into the premises under a 'licence to occupy' but any more permanent arrangements relating to the assignment or grant of an actual lease were subject to negotiations with landlords. The Acquired Stores had a number of different landlords and prospective tenants (including HMV) had to negotiate with the relevant landlord for each of the stores (in addition to, where relevant, negotiating with the administrator).

16. The overall substance of the various arrangements in relation to the Acquired Stores is that they have changed from being Zavvi stores to being traded by HMV. In relation to each of the stores, HMV informed the OFT that it has acquired the fixtures and fittings and has taken over responsibility for the staff in them (on the basis that the TUPE<sup>8</sup> regulations either clearly apply, or, in some cases, HMV consider that they might apply). HMV will also inherit any goodwill that attaches to the stores through their past trading as entertainment stores under the Zavvi brand, although the OFT understands that consideration has not been paid to Zavvi or to the administrator by HMV in relation to all stores (the position varies between the stores). In a number of cases (but not all), existing stock has also been acquired by HMV.
17. The OFT views the transfer of the leases (on the same terms as the landlords had with Zavvi), or the grant of new re-negotiated leases with the landlords, as an integral part of the overall transfer of the Acquired Stores to HMV. In line with its decision in the Cineworld case,<sup>9</sup> the fact that different components that may collectively constitute an enterprise (property, stock, fixtures and fittings, goodwill, employees) are acquired from different parties does not negate this conclusion.
18. As a result, the OFT believes that it is or may be the case that the Acquired Stores each constitute enterprises for the purposes of consideration under the Act.
19. The OFT accepts that this conclusion is stronger in relation to certain of the Acquired Stores than in relation to others. In particular, in relation to the Manchester Arndale store, the OFT considers that this particular situation qualifies for examination only on the basis that it 'may be the case' that a relevant merger situation has been or will be created.<sup>10</sup> The

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<sup>8</sup> Transfer of Undertakings (Protection of Employment) Regulations 2006, SI 2006/246.

<sup>9</sup> Anticipated acquisition by Cineworld Group plc, through its subsidiary Cine-UK Limited, of the cinema business operating at the Hollywood Green Leisure Park, Wood Green, decision of 17 March 2008.

<sup>10</sup> In Manchester Arndale, a third party (Head) had in fact temporarily traded from the store during the intervening period between Zavvi's entry into administration and HMV's entry into the store. Further, HMV acquired no stock from Zavvi/the administrator or Head and paid no consideration to Zavvi/the administrator, and HMV stated there was also a question mark over its legal responsibility (i.e. under the TUPE regulations) for taking on the ex-Zavvi employees. However, set against this, HMV did in fact take on the employees in the store and did acquire the fixtures and fittings with the store. It would also inherit any goodwill that still attached to the store; even if there were to be a temporary interruption in the identity of the leaseholder,

OFT notes that, in any event, whether Manchester Arndale is treated as a relevant merger situation or is excluded from investigation under the Act does not alter the OFT's overall conclusion – for the reasons given in the remainder of the decision – not to refer the aggregated acquisition of the Acquired Stores by HMV to the Competition Commission.

20. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

#### **Application of section 27(5) of the Act**

21. The Acquired Stores were acquired by HMV at different times (as discussed above). In addition, to some extent, different parties were involved in supplying the different components that collectively led to the transfer of the stores from Zavvi to HMV in the different locations, that is, the different landlords of the stores, and in one case (Manchester Arndale) a third party as a temporary occupier.<sup>11</sup>
22. Subject to a two year limit, section 27(5) of the Act gives the OFT the discretion to treat earlier acquisitions between the same parties or interests as having occurred simultaneously on the date on which the latest of them occurred. Section 27(8) of the Act states that, 'In deciding whether it is appropriate to treat arrangements or transactions as arrangements or transactions between the same interests the decision-making authority shall, in particular, have regard to the persons substantially concerned in the arrangements or transactions concerned'.
23. In this case, the OFT considers it appropriate to exercise its discretion under section 27(5) to treat together all of the 15 Acquired Stores, notwithstanding that different landlords were involved and there was a temporary intervening third party in one of the stores. This is because the transactions collectively arose from the recent entry into administration of Zavvi and because, in the OFT's view, Zavvi/the administrator, on the one

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customers' overall perception will be that the operation of the store as an entertainment retailer would have been continuous in essence, despite any transient changes in signage.

<sup>11</sup> The OFT was only made aware of this one case (Manchester Arndale) where a third party had temporarily occupied the store during the course of its investigation. Even if, contrary to its findings, there had been a similar occurrence at other stores, the OFT's analysis of section 27(5) would equally apply to those stores.

hand, and HMV, on the other hand, were the persons substantially concerned in all of the arrangements.

## **COMPETITIVE ASSESSMENT**

24. The circumstances of this case, namely that Zavvi had entered into administration, self-evidently raise the question of whether the appropriate counterfactual to this merger was indeed the ongoing presence of Zavvi as a competitor in each of the Acquired Store locations.
25. In its Tesco/Kwiksave decision<sup>12</sup> the OFT asserted that its general approach is to rely on pre-merger conditions as the appropriate proxy for the counterfactual and to 'test' the competitive impact of any transaction against such a standard before proceeding to consider whether another counterfactual should be substituted. This gives effect to the principle that it is generally appropriate to engage in a counterfactual analysis (that is, to consider whether it is appropriate to depart from the 'default' pre-merger conditions of competition) only where the OFT believes that the merger would in fact otherwise create competition issues.
26. In this case, the OFT considered whether the acquisition by HMV of the Acquired Stores had the potential to give rise to prima facie concerns. On a cautious basis, the OFT considered that an appropriate candidate frame of reference could be the bricks and mortar retailing of entertainment products including pre-recorded music, films, electronic games and peripherals on both a national and local basis. In line with previous decisional practice, the OFT considered that its starting assumption would be that competition takes place at a local as well as national level. Accordingly, given the OFT's experience in looking at local competition in potentially analogous retail cases, and on a cautious basis, a candidate local frame of reference could be taken as a one mile radius around a Zavvi store.
27. Based on this approach, relative to pre-merger conditions of competition, no issues arise on a national level, due to the very limited increment that would arise as a result of the transaction. However, on a local level, overlaps with an existing HMV store would arise in seven of the 15

locations – Peterborough, Plymouth, Southend, Glasgow Buchanan Galleries, Croydon, Nottingham and Manchester Arndale (collectively the Overlap Stores). The OFT does not consider that competition concerns would arise in relation to the other eight Acquired Store locations on even the most cautious assessment as HMV does not operate stores near to these sites prior to the acquisition.

28. Given that prima facie competition concerns may arise in relation to the seven Overlap Stores, the OFT considered it appropriate in this case to focus on the applicability or otherwise of an exiting firm counterfactual analysis.<sup>13</sup> In the particular circumstances of this case, the OFT considered that it would be disproportionate to require the parties to carry out an in-depth analysis in relation to each of the Overlap Stores given the clarity of evidence indicating the application of the failing firm defence that the OFT was able to attain at an early stage of the investigation. This will clearly not be the case in all failing firm type situations.
29. To the extent that the OFT had concluded differently on the counterfactual, it would have been necessary for the OFT to reach a firm conclusion as to whether – given the local competitive conditions and the OFT's view of the relevant product and geographic markets – the Overlap Stores did in fact give rise to a realistic prospect of a substantial lessening of competition in the relevant local areas.

## **COUNTERFACTUAL**

### **Pre-merger conditions of competition are not the appropriate counterfactual**

30. For the reasons set out below, the OFT considers that pre-merger conditions of competition are not the appropriate counterfactual in this case on the basis that the Acquired Stores would inevitably have exited the market in the near future, and there were no other realistic substantially less anti-competitive purchasers for the stores despite the marketing efforts of the administrator and respective landlords. In particular, interest in a number of stores from a party operating within the same market were not

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<sup>12</sup> Anticipated acquisition by Tesco Stores Limited of former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson), decision of 11 December 2007, paragraph 19.



viewed by the landlord, and consequently the OFT, as meeting the 'realistic' purchaser test.

31. HMV submitted that the correct counterfactual for the consideration of the acquisition of the Overlap Stores should be that, absent the merger, Zavvi would cease to operate, at least as a retailer of entertainment products. In effect, HMV argued that to the extent competitive harm may arise, the merger is not the cause of this as it would occur in any event.
32. The OFT's position on how it will assess an exiting (including failing) firm defence was recently articulated in the 'Restatement of OFT's position regarding acquisitions of 'failing firms'', published on 18 December 2008. The OFT confirmed in that restatement that it will only clear a transaction based on 'failing firm' claims where it has sufficient compelling evidence that the following conditions are met:<sup>14</sup>
  - (i) absent the merger, the target business would have inevitably exited with no serious prospect of re-organization
  - (ii) there was no realistic and substantially less anti-competitive alternative to the merger, and

**Inevitable market exit of the Overlap Stores absent the merger with no serious prospect of re-organisation**

33. Zavvi entered into administration on 24 December 2008. However, this fact in itself was not conclusive that the first limb was satisfied. The OFT investigated carefully with the administrator whether there was any prospect that Zavvi could have emerged from administration, potentially in a re-organized form.

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<sup>13</sup> See further the OFT's treatment of evidence required to meet the conditions of its failing firm defence (Mergers: *Substantive Assessment Guidance*, paragraph 4.36-39) and Restatement of OFT's position regarding acquisitions of 'failing firms', published on 18 December 2008.

<sup>14</sup> The OFT notes, however, that the standard has been considered in previous decisional practice at first-phase and has been successful in some of these. See Completed Acquisition by Home Retail Group plc of Stores from Focus (DIY) Ltd, decision of 15 April 2008; Completed acquisition by the CdMG Group of companies of Ferryways NV and Searoad Stevedores NV, decision of 24 January 2008; Anticipated acquisition by Tesco Stores Limited of former Kwik Save stores (Handforth, Coventry, Liverpool, Barrow-in-Furness and Nelson), decision of 11 December 2007; First West Yorkshire/Black Prince, decision 27 May 2005, BAI/P&O Ferries, decision of 7 December 2004; Arcelor/Corus, decision of 9 September 2004, Taminco/Air Products, decision of 16 July 2004.

34. As noted above, the administrator informed the OFT that Zavvi had been experiencing significant losses for a number of years and that failure was a possibility even before the collapse of EUK. For the 78 weeks<sup>15</sup> to 27 September 2008, Zavvi incurred a loss of £55 million on sales of £441 million. Zavvi had a substantial excess of liabilities over realisable assets at the time of entering administration and would have required a substantial cash injection of many tens of millions of pounds to ensure it could continue to survive as a going concern. At the time of administration, Zavvi owed its main supplier, EUK, over £70 million. The administrator's view was that there was no prospect of this debt being repaid in full.
35. EUK had entered administration itself on 27 November 2008, resulting in severe disruption to supplies and substantial working capital pressures to ensure continued access to stock by Zavvi. Given the absence of any prospect of a going concern sale of EUK, the operating model under which Zavvi had worked therefore broke down and it was not possible to secure continued supplies on a timely basis, at competitive margins or on acceptable credit terms.
36. Zavvi faced quarterly rent payments aggregating circa £13 million due on 25 December 2008. The OFT was told that there was no prospect of funds becoming available from any sources to enable payment, and Zavvi therefore required immediate protection from the administration moratorium to protect value in the best interests of all creditors. As Zavvi continued to trade within administration, the business continued to incur significant overhead costs which necessitated the phased closure of stores in the absence of a transfer of those stores or sale of the business as a going concern.
37. There was a significant level of retention of title claims received from original suppliers, acting through EUK, seeking the return of stock or payment for goods previously supplied. This hindered any efforts to continue to trade the business on a break-even basis, a factor further compounded by many suppliers taking legal action.
38. The OFT was informed by the administrator that a going concern sale was not achievable for a variety of other reasons, including the difficult current economic and market conditions and the prohibitive level of investment required to turn around the Zavvi business. In particular, the administrator

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<sup>15</sup> 78 weeks was the time period for which the administrator provided the OFT with figures for losses.

told the OFT that they believed there was an absence of liquidity in funding markets to support an acquisition by trade, private equity or MBO style interest. He also considered that there was no obvious credible competitive trade interest in a purchase of the Zavvi business due to the attrition in operators in the sector in recent years.

39. In fact, at the time of HMV's first tranche of purchases, the administrator had already closed 72 Zavvi stores. The remaining Zavvi stores, other than those transferred to HMV or Head, were closed by 20 February 2009 despite the administrator's efforts to sell the stores as a going concern.
40. The OFT is therefore confident, based on all the above mentioned factors, that there is sufficient compelling evidence that the first limb of the failing firm criteria is met, i.e. the inevitable market exit of the Overlap Stores absent the merger with no serious prospect of re-organization.

#### **No realistic and substantially less anti-competitive alternative to the merger**

##### **No realistic acquisition by another music/DVD/games retailer**

41. In practice, in the specific circumstances of this case, control of the Zavvi stores partly lay with the landlords given that any prospective assignment of leases (or the grant of any new leases) had to be negotiated through the relevant landlord of each store and the administrator was not central to this process. Without landlord agreement, there could be no transaction. The OFT therefore considers that, the 'realistic purchaser' test it applies in its counterfactual analysis must take account of whether such purchasers could have been acceptable to the landlords in question.
42. The administrator set a notional deadline of 9 January 2009 for indicative offers from any interested parties for the Zavvi stores. The landlords of the Overlap Stores told us that they did not undertake a public marketing campaign for the stores given that they were city centre locations and only a limited number of parties were likely to be interested in them. Instead, they marketed selectively to parties they believed, through research or through past contact, might be interested. The administrator and the landlords also relied on the fact that the availability of Zavvi stores had been widely publicised through the media coverage of Zavvi's demise. On this basis (that is, the fact that the demise of Zavvi was widely publicised),

the OFT is satisfied that there was sufficient awareness regarding the availability of the stores to draw the attention of any prospective purchasers.

43. In relation to three of the Overlap Stores,<sup>16</sup> despite efforts by the administrator to find a purchaser, there were no expressions of interest, and as a consequence no possibility of a sale, to retailers operating in the same market as the parties ('in market' purchasers) other than HMV. Given the degree of publicity surrounding the demise of Zavvi and the evidence received from the administrator, the OFT is confident that there was therefore no other realistic purchaser for these stores and they are therefore considered clearly to satisfy both limbs of the 'failing firm' test.
44. The remainder of this analysis therefore focuses on the remaining four Overlap Stores<sup>17</sup> in relation to each of which there were 'in market' offers from Head (in addition to the winning offers made by HMV). The terms on which Head offered to take on the leases of each store were largely similar.<sup>18</sup> In all four locations the OFT was informed that Head's offer was rejected by the landlords in question.<sup>19</sup>
45. The fact that HMV's offer was commercially preferable to Head is not sufficient for the OFT to disregard Head as a realistic alternative purchaser. The question for the OFT is whether – in the absence of HMV's offer – the landlords of these four stores might realistically have entered into an ongoing agreement with Head or whether they would ultimately have preferred to leave the store empty (that is, to search for an 'out of market' purchaser to use the retail space other than for the retail of entertainment products).

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<sup>16</sup> Peterborough, Plymouth and Southend.

<sup>17</sup> Glasgow Buchanan Galleries, Nottingham, Croydon and Manchester Arndale.

<sup>18</sup> [ ]

<sup>19</sup> In relation to Manchester Arndale, the administrator gave Head a 'licence to occupy' the store before any negotiations could take place between Head and the landlord. This gave Head the ability to occupy the store, but did not assign the existing lease or constitute a re-negotiated agreement. Head occupied the store for a period of four weeks, at which point the landlord came to a long term leasing agreement with HMV and Head's occupancy was terminated. The OFT is confident that Head's interim licence should not be regarded as tantamount to an ongoing transfer and that, even absent HMV's offer, Head's occupation was regarded by the landlord as a temporary arrangement [ ]

46. The landlords in question informed the OFT that the offer they received from Head was unacceptable in absolute terms (and not simply in comparison to HMV's offer) for the following reasons:
- (i) [ ]
  - (ii) [ ] Head's short term business model
  - (iii) The landlords' objectives were to secure well known brands to take over their sites which in most cases were in prime city centre locations and by doing this improve the profile of retailers in the locations.
  - (iv) The landlords were reluctant to accept offers from 'unknown' potential tenants [ ].<sup>20</sup> [ ].
  - (v) [ ]
47. Landlords emphasised to the OFT that the only offers for the four Overlap Stores they received which they perceived as 'realistic' and therefore worthy of consideration were from HMV. In the event that HMV had not re-negotiated leases, despite the current adverse financial climate, each of the landlords' preference going forward was to keep the properties vacant and continue to market them with the understanding that it could have taken [ ] to find a suitable tenant rather than accept any other offer they had received.
48. The OFT notes by way of corroboration of the landlords' views above that Head had in total made offers for [ ] Zavvi stores to landlords, offering largely the same terms in all locations, and that in only [ ] locations had it been accepted. Out of the [ ] locations where Head's offer was rejected, in [ ] of these there was no alternative offer and the store has now been closed (the remaining [ ] of the [ ] have been leased to HMV, as discussed above). This confirms the proposition that in most instances the landlord's preference was to reject Head's offer and to continue to market the site, which would lead to the closing of the entertainment store.

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<sup>20</sup> We note, however, that Head was set up by members from Zavvi's former management (and that they clearly have prior experience of operating an entertainment store).

49. Given that the landlords of none of the Overlap Stores – including those in which Head had made an offer – would accept offers made by Head as a medium or long term proposition under any circumstances, the OFT believes that Head should not be regarded as a realistic alternative purchaser for the Overlap stores. Indeed, the OFT notes that, even in those instances where Head's offer was accepted, the landlords viewed the arrangements as an interim measure, and that they have continued to market the properties in view of (a) the poor terms on offer from Head; and (b) the short term nature of Head's business model.
50. The OFT therefore believes that there are no realistic alternative buyers whose acquisition of the Overlap Stores (or their relevant assets) would produce a substantially better outcome for competition.

#### **Closure of the Overlap Stores as a more competitive outcome for consumers?**

51. The OFT states in its Guidance that 'it may also be better for competition that the firm fails and the remaining players compete for its share and assets than that the failing firms share and assets are transferred wholesale to a single purchaser'.<sup>21</sup>
52. In this case, the OFT does not believe that the closure of the Overlap Stores and the exit of the assets in the local markets would have been a substantially better outcome than the acquisition of the stores by HMV. The post-merger outcome does not result in a reduction of competing fascia relative to the exit of the assets in any event.

#### **CONCLUSION**

53. Based on the above, the OFT does not believe that HMV's acquisition of the Overlap Stores, or indeed any of the other Acquired Stores, creates the realistic prospect of a substantial lessening of competition.

#### **THIRD PARTY VIEWS**

54. The OFT did not receive any comments from third parties who were concerned about the transaction.

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<sup>21</sup> OFT Mergers – Substantive Assessment Guidance OFT 516, may 2003, paragraph 4.37.

## **ASSESSMENT**

55. The OFT believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation in relation to the 15 Acquired Stores by HMV and that these should be treated together under section 27(5) of the Act.
56. The OFT considers that, on a cautious approach to candidate product and geographic market definitions, the merger gives rise to potential competition concerns in relation to seven Overlap Stores.
57. After careful analysis, the OFT has concluded that the normal benchmark against which merger effects are assessed, pre-merger conditions of competition, did not apply in relation to these Overlap Stores as Zavvi had exited the market. The question, therefore, is whether there could realistically have been a substantially less anti-competitive alternative to the proposed merger.
58. The OFT is satisfied that there is no realistic prospect of a substantially less anti-competitive alternative buyer for the Overlap Stores, nor of any other outcome that would be substantially better for competition than an acquisition by HMV.
59. As such, the counterfactual against which the merger must be judged in this case is a scenario in which the competitive threat from Zavvi will be lost in any event. Accordingly, the merger itself cannot be regarded as the cause of any lessening of competition.
60. Consequently, the OFT does not believe that it is or may be the case that the acquisition of the Acquired Stores by HMV may be expected to result in a substantial lessening of competition within a market or markets in the UK.

## **DECISION**

61. This merger will therefore not be referred to the Competition Commission under section 33(1) of the Act.