

CASE ME/6752/18

PARTIES' RESPONSE TO THE NOTICE OF POSSIBLE REMEDIES

Sainsbury's

J Sainsbury plc

ASDA

ASDA Group Limited

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1 Executive Summary

Asda and Sainsbury's categorically reject the CMA's view that coming together will lead to a worse outcome for customers.

We operate in a rapidly changing and competitive market, where customers have more choice than ever in how they shop for groceries. The driving force behind this merger is to deliver lower prices, better quality and service for our customers.

We will lower prices for customers by £1 billion annually by the end of the third year, starting with a first year investment of £300 million. This is a public commitment and will be substantiated by an independent third party.

The CMA's analysis ignores both the evidence and the realities of how customers shop today. The CMA has applied a threshold for identifying local areas of concern that does not fit the facts and is far below the most conservative standards applied in previous cases. This means that the CMA identifies an area of concern where an Asda and a Sainsbury's store are within seven minutes' drive time of each other, irrespective of whether there are one or six competitors in the same area. Essentially, a competition test that ignores competition.

Furthermore, the CMA's remedy proposal is impossible to implement. It is prohibition in all but name and deprives customers of lower prices, better quality and better service.

The Parties are setting out a substantial remedy package which applies thresholds that are, on any view, extreme and unprecedented as an automatic problem. The proposed divestments are attractive assets generating [X] a year, offering an opportunity to strengthen the market by allowing multiple buyers to benefit from these potential divestments.

- 1.1 This submission is made on behalf of J Sainsbury plc ("**Sainsbury's**") and Walmart Inc. ("**Walmart**"), the U.S. parent company of ASDA Group Limited ("**Asda**", and, together with Sainsbury's and Walmart, the "**Parties**") in response to the Competition and Markets Authority ("**CMA**")'s Notice of Possible Remedies of 20 February 2019 (the "**Remedies Notice**") in relation to the proposed combination of Sainsbury's with Asda (the "**Proposed Merger**").
- 1.2 The Remedies Notice identifies prohibition and divestiture as potential remedies to the concerns set out in the CMA's Provisional Findings of 20 February 2019 (the "**Provisional Findings**"). However, the provisional views contained within the Remedies Notice regarding divestiture indicate a preference for the most stringent and interventionist approach to every possible remedy parameter. These far exceed the requirements imposed in previous cases, despite the fact that those cases were considered against a backdrop of customers having less choice of where and how they shop than they do today. When read as a whole, the divestiture "remedy" presented in the Remedies Notice appears to have been designed to be impossible to implement. As such it is prohibition in all but name. Such an outcome would deprive customers of over £1 billion annually in Relevant Customer Benefits ("**RCBs**") that can be expected to arise from the Proposed Merger and which were substantiated by two independent consultants.
- 1.3 As will be set out in further detail in the Parties' response to the Provisional Findings, the number of local SLCs identified by the CMA is the result of a fundamentally flawed analysis.

After deduction of the 1% efficiency credit, the bottom line is this: the GUPPI threshold applied on a net basis is 1.5% - this is the residual amount of upward price pressure that, in the CMA's mind, proves an SLC problem. This has resulted in the CMA identifying a total of 629 local supermarket, 290 local online and 65 local convenience SLCs.

- 1.3.1** At a macro level this means that the CMA identifies an area of concern where an Asda and a Sainsbury's store are within seven minutes' drive time of each other, irrespective of whether there are one or six competitors in the same area of an equal strength to the Parties.
- 1.3.2** At a micro level this means, for example, that a local area with 10 competitor stores within an eight minute drive time, including three Tesco and Morrisons stores above 30,000 sq. ft, two Aldi stores, one Lidl, two Co-ops, one M&S, one Iceland, one 65,000 sq. ft Sainsbury's store and one 9,000 sq. ft Asda store, give rise to an SLC.¹
- 1.4** As will also be set out in further detail in the Parties' response to the Provisional Findings, the Parties fundamentally disagree with the CMA's findings that groceries ordered online and delivered to a customer's location represent a separate product market to in-store groceries. These findings are predominantly based on the CMA's online survey, which the Parties maintain is unreliable, and ignore market data and evidence from third parties. In practice, customers view grocery shopping as one market irrespective of whether they shop in-store or online and whether they have their groceries delivered to their location or pick them up in-store. In addition, this is a dynamic market, with double digit growth and continued entry and expansion. The most recent example is the M&S/Ocado joint venture.
- 1.5** As the Parties will also set out in their upcoming response to the Provisional Findings, past decisional practice, including *Tesco/Booker*, clearly demonstrates that the appropriate GUPPI level should be closer to 10%. A GUPPI threshold of 5% as a decision rule would be extremely conservative and unprecedented. However, for the purposes of our response the Parties and their advisers have calculated the SLCs that would result from a 5% GUPPI in relation to the sale of grocery items in-store (including via convenience stores) (the "**Revised In-Store SLCs**"), and online (the "**Revised Online SLCs**").
- 1.6** In light of the CMA's continued rejection of the Parties' position that a decision rule is inappropriate altogether for fuel, the Parties have calculated SLCs based on a decision rule that does not suffer from the many flaws of the two-pronged decision rule approach in the Provisional Findings. For illustrative purposes the Parties have calculated the SLCs that would result from a diversion ratio threshold of 40% (the "**Revised PFS SLCs**"). The Revised In-Store SLCs, the Revised Online SLCs and the Revised PFS SLCs are collectively referred to as the "**Revised SLCs**".
- 1.7** The table below compares the number of local SLCs that arise: (i) based on the CMA's analysis for supermarkets, convenience stores and online grocery, using a GUPPI of 2.5% (post-efficiencies) and a GUPPI of 5%;² and (ii) for fuel, using the alternative GUPPI and pricing indicators used by the CMA and an illustrative diversion ratio threshold of 40%. This demonstrates that a significantly lower number of SLCs would arise at thresholds that are more conservative than those adopted in previous UK decisional practice.

¹ This example relates to the SLC that the CMA has found in relation to the [§].

² The Parties have used the tables of SLCs at Chapter 17 of the Provisional Findings for the calculations, which are without prejudice to any further submissions in response to the Provisional Findings.

CMA Area of Concern	Number of SLCs at Intervention Threshold	
Grocery	2.5% GUPPI	5% GUPPI
Supermarkets	629	182
Convenience	65	19
Online	290	11 ³
Fuel	1.5% GUPPI / 0.75 ppl Pricing Indicator	40% Diversion
Fuel	132	38

- 1.8** The Parties have used this analysis as the basis for a proportionate and effective remedy proposal (the “**Proposed Remedy Package**”), which consists of local structural divestments to solve the Revised In-Store SLCs and Revised PFS SLCs as follows:
- 1.8.1** the divestment of 125-150⁴ supermarkets and a number of convenience stores to one of the Parties’ current competitors or a new entrant to the market; and
- 1.8.2** the divestment of a sufficient number of petrol filling stations (“**PFS**”) to either grocery buyers, where they are sold with a grocery divestment store to remedy a Revised In-Store SLC, or, where they are not, to an existing fuel operator who will operate a low price, high volume model, underpinned by contractual incentive mechanisms where required.
- 1.9** Taken together, these proposals represent a unique opportunity for existing operators to add additional scale or for a new operator to obtain immediate scale. The Proposed Remedy Package will result in divestments of assets generating over £[~~3~~] million of cash flow, higher than the profits delivered by businesses like Iceland and Coop Food, and at least £[~~3~~] billion of sales.
- 1.10** Further, in relation to online grocery, the Parties strongly believe that a remedy is not necessary or proportionate, but would be willing to discuss possible solutions to any residual concerns with the CMA.
- 1.11** Moreover, synergies generated by the Proposed Merger will enable the Parties to make the following commitments (the “**Public Commitments**”):
- 1.11.1** Investing £1 billion annually in lower prices across Asda and Sainsbury’s by the third year following completion of the Proposed Merger, with £300 million invested in the first year post completion; and
- 1.11.2** Sainsbury’s implementing a cap on fuel gross profit margin above cost of 3.5 pence per litre at all Sainsbury’s fuel locations for a period of five years post-merger. Asda will continue to maintain its current low-cost price policy.
- 1.12** To ensure the Parties will deliver on the Public Commitments, they will appoint an independent third party, to monitor and report on their actions.

³ This has been calculated on the basis of the margins used by the CMA in its GUPPI calculations. The Parties will present corrected margins in the response to the Provisional Findings.

⁴ The range reflects the fact that the precise number of stores required to remedy local SLCs depends on the purchaser/s in question.

1.13 The Proposed Remedy Package meets the criteria for effectiveness set out in the CMA's Merger Remedies Guidance⁵ (the "**Remedies Guidance**") and preserves RCBs in a way that prohibition and the divestiture requirements of the Remedies Notice do not. The Public Commitments demonstrate the Parties' commitment to realising and passing on to customers the substantial variable cost and other synergies which will result from the Proposed Merger and which the CMA has, exceptionally, in this merger acknowledged.⁶

2 CMA proposals are disproportionate

Prohibition would be disproportionate

2.1 The Remedies Guidance states that "[i]n order to be reasonable and proportionate the [CMA] will seek to select the least costly remedy, or package of remedies, that it considers will be effective"⁷ and that "the [CMA] will seek to ensure ... that no remedy is disproportionate in relation to the SLC and its adverse effects".⁸ The same principles are reflected at paragraph 3.3 of the CMA's updated Remedies Guidance published on 13 December 2018 ("**Updated Remedies Guidance**").⁹ The CMA has an important and overarching duty to act in a manner that is reasonable and proportionate when conducting a merger review and considering remedies.¹⁰

2.2 In the present case, the CMA is faced with two types of remedies that would comprehensively and effectively address the SLCs identified and any adverse effects, namely prohibition and divestiture:

2.2.1 Prohibition would be disproportionately costly and intrusive. It is the most extreme form of remedy and would prevent the Proposed Merger from taking place. This would result in the Parties being less effective competitors in the market than they would be should the Proposed Merger proceed. Most importantly, it would prevent realisation of independently calculated and substantiated efficiency savings of £1.6 billion (of which £1 billion has been substantiated to a Quantified Financial Benefits Statement ("**QFBS**") standard)¹¹ and as such prevent the significant reductions in prices to be made by the Parties as a result of the Proposed Merger and corresponding market-wide improvements in rivalry as a result. Therefore, prohibition of the Proposed Merger would result in a significant loss of customer benefits. As set out in section 35(5) of the Enterprise Act 2002 (the "**Act**") and in paragraph 1.15 of the Remedies Guidance, "*RCBs that will be foregone due to the implementation of a particular remedy may be considered as costs of that remedy by the CMA. The CMA may modify a remedy to ensure retention of an RCB or may*

⁵ Competition Commission, Merger Remedies: Competition Commission Guidelines, November 2008, which according to the CMA website applies to Phase 2 merger investigations that commenced prior to 13 December 2018, paragraph 1.8.

⁶ The Parties dispute the quantum of efficiencies the CMA provisionally finds.

⁷ Remedies Guidance, at paragraph 1.9.

⁸ Remedies Guidance, at paragraph 1.7.

⁹ The CMA's Updated Remedies Guidance is applicable to mergers referred to Phase II after this point.

¹⁰ The relevant public law principles are very well established and long-standing. For a description of their key features see: *Huang* [2007] 2 AC 167, paragraph 19; *Eastside Cheese* [1999] Eu LR 968, paragraph 41 and *International Transport Roth GmbH* [2003] QB 728, paragraph 52. For the Competition Appeal Tribunal's interpretation of what the principle of proportionality requires in the context of remedies, please refer to Competition Appeal Tribunal's statements in *Tesco plc v Competition Commission* [2009] CAT 6, paragraph 137.

¹¹ A QFBS is a quantified statement of synergies expected from a proposed acquisition, made by an offeror; or a statement by an offeree company quantifying any cost saving or other financial measures that it proposes to implement if a contested offer is withdrawn or lapses, which is required under Rule 28 of the Takeover Code.

change its remedy selection. For instance, it may decide to implement a remedy other than prohibition."¹²

- 2.2.2** For the reasons set out below, the Proposed Remedy Package would be an effective and comprehensive means to remedy SLCs, both local and national, across all theories of harm.
- 2.3** The CMA has also raised concerns in the Remedies Notice that allowing the Proposed Merger to proceed, even with extensive divestitures, would represent a major restructuring of the UK groceries sector and its market dynamics.
- 2.4** However, the CMA would be acting disproportionately and unreasonably were it to prohibit the Proposed Merger on this basis. A change in market structure is not *per se* a reason to prohibit a merger because all mergers and acquisitions bring about changes in market structures, and it is not uncommon in either previous UK or current EU practice for material remedies packages to be both required by competition authorities and to be implemented.¹³ The mere reference to undefined "*weaker competitive pressures across the markets where the Parties operate*" is not sufficient: the CMA does not provide any reason to show how such undefined concerns could prevent a divestiture package from remedying the SLCs identified.¹⁴
- 2.5** As regards the CMA's concern that divestiture may impact the ongoing operations of the Parties, the Parties are confident that a sensibly structured divestment package (as further described below) would not damage their ability to continue to act as an effective and vigorous competitor. Indeed, by allowing the Proposed Merger to proceed and thus the significant efficiencies to be achieved, the Proposed Merger would create a more competitive entity and prompt greater rivalry in the market as a whole, as shown by the adverse reaction of the Parties' major competitors to the Proposed Merger.

The divestiture remedy as framed by the CMA is disproportionate

- 2.6** The divestment remedy as set out by the CMA in the Remedies Notice is entirely disproportionate. The scope of the conditions imposed in order to achieve the remedy is unworkable and effectively equivalent to prohibition. As discussed in more detail below, the remedy is unprecedented in the way it is framed and disproportionate to the aim of solving any credible SLCs that could be expected to arise as a result of the Proposed Merger.
- 2.7** In particular, it is plainly not necessary for a proposed purchaser of any divested assets to provide "multi-channel" or similarly integrated operations to those of the Parties. So long as the assets included in a remedy package are sufficient to allow the purchaser to effectively compete in the *relevant market in which an SLC has been identified* on an ongoing basis, the remedy will be effective and sufficient to address the competition concerns identified by the CMA with respect to the Proposed Merger. In this respect, the CMA has not identified a

¹² Paragraph 3.16 Updated Remedies Guidance. See for example the CC investigation into Macquarie UK Broadcast Ventures of National Grid Telecoms Investment Limited (2008). The CC concluded that a package of behavioural remedies addressed the adverse effects of the merger (a merger to monopoly) and would pass back to customers a significant proportion of the relevant merger synergies and substantial compensation in lieu of the loss of future competition.

¹³ For example, in *John Wood Group/Amec Foster Wheeler*, the Parties' divestiture package was worth £228 million, compared to the £1.97 billion value of the retained business; in *AB InBev/SABMiller*, the Parties made \$16.5 billion of divestments, relative to an approximate retained business value of \$90.5 billion; in *Linde/Praxair*, the Parties divested over \$9 billion of assets, relative to a retained business value of approximately \$37 billion. Proportionately, these divestments represent a significantly greater share of the acquired business than would be necessary to remedy credible and evidence-based SLCs in this case.

¹⁴ Section 36(1) of the Act.

bundled market for grocery, fuel or general merchandise in the Provisional Findings and the evidence supports the fact that any “halo effect” is small. The CMA has investigated the effects of the Proposed Merger “*under a number of distinct theories of harm, related to distinct activities or product areas where the Parties overlap*”.¹⁵

- 2.8** Nor has the CMA articulated a theory of harm that the Parties are active in separate markets involving complementary products or services. It has also acknowledged in the Provisional Findings that several competitors exercise significant competitive constraints within the relevant markets concerned which are not “multi-channel” retailers. For example, Aldi and Lidl are strong competitors for in-store groceries but have no online grocery or fuel offerings in the UK, whilst Ocado is a successful online-only competitor and seen by the CMA as a key constraint.

3 Divestiture to remedy local SLCs will also address any national concerns

- 3.1** The divestiture of a package of stores that comprehensively addresses competition concerns ultimately identified in the local areas in which the Parties compete would also comprehensively address any national SLC concerns. This is because, as set out in previous submissions and as the CMA reflects in its Provisional Findings,¹⁶ “*national competition is the sum of local competition*”. To the extent that the Parties’ incentives (e.g. to degrade PQRS) following the Proposed Merger are not significantly altered in a significant proportion of the local areas in which they compete, then their incentives at the national level will also not significantly change. Divestments designed to address SLCs at a local level will thus remove all competition concerns ultimately identified (whether at the local or national level).
- 3.2** As noted by the CMA in the Provisional Findings, competition for the supply of in-store groceries takes place at the local level. The CMA has correctly noted in the Provisional Findings that competition concerns across the Parties’ national supermarket store estates would only arise if “*the merger may be expected to result in competition concerns in local areas representing a significant proportion of the Parties’ overall supermarket estates*” and that any such deterioration in PQRS across the Parties’ estate as a whole would reflect “*the aggregate effect of the competitive constraints that the Parties face in each of the local areas where they operate*”.¹⁷
- 3.3** It therefore follows that this national theory of harm would be addressed by local remedies. In *Ladbrokes/Coral*, the CMA granted clearance conditional upon a divestiture remedy, which would “*involve Ladbrokes and Coral divesting sufficient betting shops to one or more suitably qualified purchasers to address the SLC that the Parties found in 642 local markets, as well*

¹⁵ Provisional Findings, paragraph 6.19.

¹⁶ See, for example, paragraph 24 of the Executive Summary of the Provisional Findings, and paragraph 7.2.

¹⁷ Paragraph 8.9 of the Provisional Findings and paragraph 24 of the Executive Summary of the Provisional Findings. In this respect the CMA refers again to paragraphs 1.13 to 1.17 of the CMA’s Retail Mergers commentary (CMA62) which states, amongst other things, that: “*A retailer will take account of the extent of local competition faced by its stores when making decisions regarding prices and other competitive variables, even if these are set uniformly across all stores. The total effect of any change in the retail offer is determined by the aggregate change in competitive conditions across all individual stores operated by that retailer. This, in turn, depends on the local competitive conditions faced by each store. [...]*”

as the SLC at the national level resulting from the aggregated loss of competition at the local level".¹⁸

- 3.4** Similarly, if the Parties address the CMA's national theory of harm with respect to in-store grocery, then the CMA's national theory of harm with respect to online parameters of competition which are set uniformly across the Parties' online and in-store offerings and with respect to Asda's convenience stores (which charge the same prices as its supermarket stores) would also fall away. With respect to parameters that are specific to online delivered groceries, as discussed below, the Parties strongly believe that a divestiture remedy is not necessary or proportionate, but would be willing to discuss possible solutions to any residual concerns with the CMA.

4 The Parties' Proposed Remedy Package and the Public Commitments

- 4.1** The CMA's Remedies Guidance indicates that a remedy will be effective where it: (a) addresses the SLC and its adverse effects by restoring the process of rivalry; (b) addresses the SLC effectively throughout its expected duration; (c) is capable of effective implementation, monitoring and enforcement; and (d) has a high degree of certainty of achieving its intended effect.¹⁹
- 4.2** For the reasons outlined above in the executive summary, and without prejudice to the Parties' further representations in the response to the Provisional Findings, the Parties and their advisers have calculated the Revised SLCs, which reflect extremely conservative and unprecedented decision rule thresholds, when compared to previous UK decisional practice.
- 4.3** The Parties set out below the Proposed Remedy Package which addresses a more credible finding of SLCs. The Proposed Remedy Package meets the criteria for effectiveness set out in the Remedies Guidance and better reflects the CMA's past decisional practice for retail mergers. In addition to local structural divestments (accepted by the CMA as solving SLCs in previous retail mergers), the Parties are also willing to offer a series of public commitments which are possible because of the substantial variable cost and other synergies which will result from the Proposed Merger and demonstrate the Parties' commitment to realising and passing on those synergies.
- 4.4** The Proposed Remedy Package includes:
- 4.4.1** the divestment of 125-150²⁰ stores (plus a number of convenience stores) to solve 182 supermarket and 19 convenience Revised In-Store SLCs on the basis of a 5% GUPPI threshold; and
 - 4.4.2** the divestment of a sufficient number of PFS to solve the Revised PFS SLCs that may result from a more reasonable decision rule (to the extent that these are not already incidentally resolved by the grocery store divestments set out above) to buyers who will operate a low price, high volume model, underpinned by contractual

¹⁸ *Ladbrokes/Coral*, paragraph 14.13. See also the decision of the OFT in *Global/GCap*: "The OFT has not found it necessary to conclude whether the merger gives rise to a realistic prospect of a substantial lessening of competition at a national level (through the creation of market power in the [two regional areas giving rise to SLC concerns i.e.] East and West Midlands). This is because, even if this were the case, the OFT considers that any remedies offered in the East and West Midlands area that are sufficient to address comprehensively the substantial lessening of competition in those regions would alleviate also any issues arising as a result of the merger at the national level".

¹⁹ Remedies Guidance, paragraph 1.8.

²⁰ The range reflects the fact that the precise number of stores required to remedy local SLCs depends on the purchaser/s in question.

incentive mechanisms in relation to each divestment PFS, if required. The Parties would expect this to amount to around 38 SLCs if a 40% diversion ratio threshold were applied (which is conservative even relative to Phase I decisional practice since the first large-scale fuel retailing merger in the Enterprise Act era (i.e. *Shell/Rontec*, 2012).²¹ Many of these SLCs will already be resolved by the proposed grocery divestments.

4.5 In relation to online delivered grocery, the Parties strongly believe that a divestiture remedy is not necessary, nor proportionate, but would be willing to discuss possible solutions to any residual concerns with the CMA.

4.6 In addition to the remedies offered by the Parties as part of the Proposed Remedy Package above, the Parties are prepared to make the Public Commitments that are possible because of the synergies that will arise as a result of the Proposed Merger. These benefits of the deal for customers will be lost if the CMA prohibits the Proposed Merger, or imposes a disproportionate or unworkable remedies package.

4.6.1 The Parties will commit to investing £1 billion annually in lower prices across Asda and Sainsbury's by the third year following completion of the Proposed Merger, with £300 million invested in the first year post completion, prior to the synergies being realised (the "**Customer Price Reduction Commitments**").

4.6.2 The Parties will commit to appoint an independent third party to substantiate that the Parties are delivering the Customer Price Reduction Commitments.

4.6.3 With respect to fuel, the Proposed Merger does not involve any departure from the current pricing strategy each Party has for the sale of fuel. It is widely recognised that Asda has a long heritage of offering low fuel prices and its customers value this position. Therefore, Asda's current fuel pricing policy will not change as a result of the Proposed Merger. In order to demonstrate their confidence in the synergies that will arise from the Proposed Merger in relation to fuel (as previously explained to the CMA) the Parties are willing to commit to a cap on the gross margin of fuel sold under the Sainsbury's banner, to confirm that customers will benefit as a result of the Proposed Merger. Sainsbury's will commit to sell fuel at a price such that no Sainsbury's site would make gross profit of more than 3.5 pence per litre on fuel (regular unleaded and regular diesel) for a period of five years post-merger ("**Sainsbury's Fuel Margin Cap**").

4.6.4 Compliance with this cap would be substantiated by an independent third party. Given UK Government initiatives on green energy and reducing harmful emissions through policies such as reducing the use of diesel engines²² the Parties consider

²¹ In *Shell/Rontec*, there were 68 overlap areas and a diversion ratio of 40% was used as the screening threshold. Areas below that threshold were automatically cleared, and areas above investigated further. Ultimately, the OFT only found SLCs in areas with diversion ratios above 50%.

²² As described in the Merger Notice, the UK fuel retailing industry is increasingly being affected by environmental concerns and the move away from fossil fuels. Following the recent concerns about diesel emissions, the UK Government has imposed a diesel car tax, in an effort to dissuade customers from using diesel vehicles, and a number of car manufacturers have announced that they will no longer sell diesel cars in the UK. Further, the Government is investing in electric vehicles in an effort to address its commitments under the Climate Change Act 2008 and has pledged to ban the sale of both petrol and diesel vehicles by 2040. These developments will inevitably result in significant changes to the demand for fuel in the medium term and therefore a 10 year review (as would be the case with an undertaking given to the CMA) does not seem appropriate.

that it would be proportionate for the Sainsbury's Fuel Margin Cap to be reviewed after five years of operation.²³

- 4.7** The above Public Commitments are only made possible by the benefits (including overhead cost savings) expected to result from the Proposed Merger. The Proposed Remedy Package will result in divestments of assets generating over £[~~£~~] million of cash flow and at least £[~~£~~] billion of sales. In addition, the Public Commitments underscore the Parties' intention to invest over £1 billion annually in groceries and fuel. Each of these remedies and the Public Commitments is assessed in further detail in the sections that follow.

5 Solving in-store grocery SLCs

- 5.1** The Parties propose to divest one or more stores, such that each Revised In-Store SLC area no longer raises an expectation of an SLC to the balance of probabilities standard. The Parties note that this will clearly and comprehensively remove any credible finding of an SLC, applying the approach outlined in paragraph 1.5 above. In previous grocery and other retail cases, such an approach has been acceptable to the CMA.
- 5.2** In *Ladbrokes/Coral*, the CMA found that an effective remedy would be one in which “*following divestment of the LBO(s) proposed in any given local area, we would not find an SLC in that local area on the basis of the approach taken in our substantive assessment (including the WSS methodology)*”.²⁴
- 5.3** The same approach should apply in the present case. Divestment of the centroid store or an alternative store selected by the Parties which brings the GUPPI estimate in a given local area below the extremely conservative and unprecedented intervention threshold of 5% is sufficient to resolve the SLC.
- 5.4** As will be set out in the Parties' response to the Provisional Findings, no remedy should be required in relation to the Parties' convenience store estates. The divestiture of supermarket stores will remedy SLCs in each local area, and as national competition is the sum of local competition, this will mean that there can be no concern in regard to the pricing of items in convenience stores, given Asda follows a single price file with its supermarkets.
- 5.5** In terms of local analysis, the Parties note that in the CMA's analysis of *Tesco/Booker*, with regard to the horizontal overlap between the Parties' convenience estates – i.e. where there is a direct and immediate read across to the theories of harm outlined by the CMA in this case at paragraphs 8.262 to 8.295 of the Provisional Findings, stores that were under a GUPPI threshold of 5% were not found to be problematic. To require convenience store disposals at a threshold of 1.5% before efficiencies as in the Provisional Findings holds the Parties to a different standard without justification, as will be set out in the Parties' response to the Provisional Findings.
- 5.6** Without prejudice to the response to the Provisional Findings, should the CMA continue to find local SLCs in relation to convenience stores, the Parties would be prepared to remedy convenience SLC areas that would arise on the application of a more reasonable GUPPI threshold. The submissions set out below in relation to in-store grocery apply equally to the proposed convenience store divestments.

²³ Reference to Platts data could be used as the best industry recognised standard for the commodity price.

²⁴ *Ladbrokes/Coral*, Final report, paragraph 14.80.

The remedy would be effective

5.7 Each store would be sold to a purchaser that meets the CMA's suitability criteria under the Remedies Guidance (see section 8 below). A divestiture package of this nature would meet each of the CMA's criteria for effectiveness:

5.7.1 Divestiture of stores to a suitably qualified purchaser or purchasers will result in an enduring structural change to each local market, restoring the process of rivalry that the CMA considers may be lost as a result of the Proposed Merger.

5.7.2 Divestment will comprehensively and effectively remedy each Revised SLC area because each area will, as a result of the divestment, be below a conservative threshold for identifying an SLC and would thus be "cleared" on a substantive review. Further, as a structural remedy, divestment will address the SLCs on a permanent basis.²⁵

5.7.3 Store divestments can be effected quickly (within the standard six-month timeframe allocated for divestiture remedies) and will act immediately upon subsequent transition of the stores to the new buyer to address the Revised SLCs. As a structural remedy, divestiture will require no ongoing monitoring and can be enforced easily.

5.7.4 By selling stores to an independent competitor who meets the CMA's purchaser criteria, the proposed divestitures are certain to achieve their intended effect. The ability of the Proposed Remedy Package to address national concerns is dealt with in section 3.

Additional assets are not required

5.8 Potential purchasers who already operate in the retail sector have the necessary supporting infrastructure, IT systems and central operations to effectively operate additional stores, together with experience in transitioning stores from previous sales processes. For new entrants to the UK grocery sector, including private equity-backed management teams with a track record in the UK grocery sector, the Proposed Remedy Package, which includes an estate of 125-150 supermarkets, and divestitures to remedy 19 convenience SLC areas and additional fuel SLCs (a total of approximately 4.5 million sq. ft.), represents an attractive opportunity for immediate scale. The Parties would offer to put in place transitional service arrangements in order to allow any new entrant time to replicate the necessary logistics and infrastructure to operate the divested stores. The Parties also note that distribution and logistics capability is widely provided by third parties and that, indeed, the Parties themselves use third-party logistics providers to service their estates.²⁶ There is an active and growing wholesaler market with operators, such as Booker (Tesco), Nisa (Co-op) and Morrisons who would be able to provide a new entrant with scale buying and support.

5.9 The CMA has not required the Parties to sell other assets in previous retail cases where large-scale and complex local divestments were required, such as *Ladbroke's/Coral* and *Somerfield/Wm Morrison*. The number of local divestments that would be required under the Proposed Remedy Package is significantly less than the number required in *Ladbroke's/Coral* and, therefore, to impose an additional requirement to sell other assets

²⁵ Divestment of grocery sites will have immediate effect to address the identified local grocery SLC, and last throughout the duration of the identified SLC, either through a permanent sale or a very long lease or sub-lease (i.e. 25 years). The CMA has previously accepted the sale of a freehold interest or, at the CMA's discretion, the grant of a long-term lease (25 years) or assignment or sub-let of a leasehold interest.

²⁶ [X]

such as supporting infrastructure, IT systems or central operations would be disproportionate and costly.

- 5.10** Further, the Parties submit that it would be disproportionate to require them to sell additional assets or operations, whether inside or outside the Revised SLC areas, to exploit economies of scale or density in purchasing or distribution. As discussed above, divestiture of a package of stores that comprehensively address any local SLCs will also comprehensively address any national SLCs.
- 5.11** In addition, there are numerous examples of successful regional operators in the UK (e.g. Booths, Henderson, Dunnes Stores) and operators who have built scale through significant store rollout programmes (e.g. Aldi, Lidl) and, therefore, the ability to exploit immediate economies of scale is not a prerequisite to operating successfully in the UK grocery market. In any event, it should be the purchaser, as opposed to the CMA, who indicates the requirements for any divestment package.
- 5.12** Finally, if a grocery store is divested to remedy a Revised In-Store SLC (but there is no accompanying Revised PFS SLC) the co-located PFS does not necessarily need to be sold to the same purchaser as the grocery store, but could be sold to a third-party fuel operator.

The Parties should be able to choose which stores and PFS to sell, including “mix-and-match” divestitures

- 5.13** The CMA and its predecessors have typically allowed merger parties the flexibility to select the stores/outlets for divestiture in retail cases. Indeed, the Competition Commission (“CC”) was clear in *Somerfield/Wm Morrison* that, subject only to the SLC being remedied in each local area, “*Somerfield should initially be required to dispose of either the acquired or the existing store...as it may choose*”.²⁷ In *Asda/Netto*, the Office of Fair Trading (“OFT”) accepted Asda’s choice as to the stores that were divested. In other retail cases, the parties have also been allowed flexibility in choosing the sites to divest, including through “mix-and-match” divestitures, for example the CMA’s decisions in *Original Bowling/Bowlplex* (2015) and *Green King/Spirit* (2015), the CC’s decision in *Cineworld/City Screen* (2013) and the OFT’s decisions in *Betfred/Tote* (2012), *Travis Perkins/BSS Group* (2011), *Cooperative Group/Somerfield* (2008) and *William Hill/Stanley* (2005).
- 5.14** Similarly, in *Ladbrokes/Coral*, the CMA found that “*the requirement of the remedy process is to identify a remedy which addresses the SLC finding or any resulting adverse effect. In that connection, when considering a number of options for disposals, it is not generally for the CMA to identify a particular choice of option. In particular where identification of the remedy is complex, the Parties and their advisers should be better positioned to undertake the practical aspects of identifying LBOs for disposal subject to the CMA’s approval.*”²⁸ The CMA therefore considered that it would be effective for the Parties to propose the licensed betting offices (“LBOs”) for divestiture in each local area. The only limitations imposed were that the stores should not have certain characteristics that put them at risk of closure (such as negative profitability, lease expiry issues or likely problems with landlord consent).
- 5.15** This is also reflected in the CMA’s Updated Remedies Guidance, which provides that “*in appropriate cases, the CMA may be willing to leave open to the merger parties which of the*

²⁷ *Somerfield/Wm Morrison*, Final Report, paragraph 11.21.

²⁸ *Ladbrokes/Coral*, Final report, paragraph 14.76.

*overlapping businesses they wish to sell, with the UILs or Final Undertakings stipulating that one of them must be sold”.*²⁹

- 5.16** There is no reason to depart from this practice in the present case.
- 5.16.1** The identity of the grocery stores that are selected for divestiture in each local area (and whether they form part of a larger package) does not affect the remedy’s ability to address the SLC in that area. The only requirement is that as a result of the proposed divestment package, the SLC is addressed. The CMA should, therefore, be agnostic as to the stores that are divested provided that this condition is met.
- 5.16.2** As there could be a number of options in terms of the stores that are capable of effectively remedying the SLC in a given area, it would be disproportionate for the CMA to select the specific stores to be divested. This would be unnecessarily restrictive and would add cost and complexity to the process, contrary to the proportionality principles of the Remedies Guidance and Updated Remedies Guidance.
- 5.16.3** There are no material composition, purchaser or asset risks that would justify a different approach. The CMA retains control over the decision on whether the buyer of each package of stores has the requisite “capability” to run the store as an effective competitor in each local market. Thus, provided the stores are of interest to a suitable purchaser, the CMA should have no concerns about their effectiveness.
- 5.17** There are also a number of important practical reasons why the Parties should be allowed to select the stores to be included in the divestiture package.
- 5.17.1** It is important that the Parties retain flexibility in their ability to conduct a sound sale process. The specific composition of each package will affect the pool of purchasers that may be able to acquire it. For example, a purchaser may not be able to acquire a specific store in a given area, because it may raise prima facie competition concerns due to an overlap with that purchaser’s existing stores. However, a nearby alternative store may be equally effective in remedying the SLC without raising any concerns for the purchaser. This is particularly relevant given the CMA’s preference for purchasers to have “scale”, as this will raise the likelihood that the purchaser will already be present in a local area.
- 5.17.2** Similarly, there may be stores that solve more than one SLC, but that can be purchased only by one particular purchaser. If this purchaser were to choose not to do so, the Parties may need to sell alternative stores in order to eliminate the SLC identified by the CMA. The approach to the sale of stores therefore needs to be flexible and dynamic so that these kinds of decisions can be made at speed.
- 5.18** It would be extremely difficult for the CMA to identify the “smallest viable” package of assets, in circumstances where it has to choose between various options of store divestitures that are each capable of remedying the SLC identified in a given area, without very detailed (and rational) rules to define the criteria for deciding which stores and PFS to divest in each case. This would place an undue burden on the CMA’s time and resources. The Parties are in the best position to evaluate the viability of a divestment package and make a proposal to the CMA on that basis. The CMA will then have the ability to test and assess the suitability of that package.

²⁹ Updated Remedies Guidance, paragraph 5.6.

- 5.19** Furthermore, there should be no concerns that “mix-and-match” divestiture packages of the Parties’ stores (including in relation to online Supply Points) and PFS would not be able to operate effectively. By their very nature, the Parties’ store estates – and those of their competitors – typically encompass a variety of store formats and profiles, having been built up by many piecemeal acquisitions of individual stores and store packages over time. Irrespective of its present branding and operator, a grocery store is fundamentally a grocery store and, as the CC recognised in *Somerfield/Wm Morrison*, there is usually “*little material difference in the characteristics of the acquired and existing store*”.³⁰ Therefore there is no basis for identifying composition risks in relation to the Proposed Remedy Package.
- 5.20** Moreover, to the extent that purchasers of divested stores are existing retailers with existing store estates, they will be readily able to integrate new stores. All trading grocery stores share more common elements than differentiation between operator models: they generally all have a customer entrance off a car park or high street, a regular sales floor shape and layout with checkouts at the front, ambient fixtures and refrigeration units on the sales floor and a back of house/warehouse for the storage of stock and colleague areas. Differentiation in grocery stores is mainly limited to branding, signage and front of house operations (checkouts). All of these can be changed in a short period of time and with limited capex investment from a new operator and all retailers have the ability to flex their models to different stores.
- 5.21** For example, during the integration of Netto into the Asda network, the only changes were that grocery stores were re-branded, new signage erected and modifications made to the front of house operations. In addition, Sainsbury’s acquired 12 Safeway stores in 2004/5 and converted them to Sainsbury’s stores within 3-4 weeks largely due to retaining most of the fixtures and infrastructure i.e. refrigeration, shelving, warehouse chillers, checkout podia, car parks etc.

6 Solving online grocery SLCs

- 6.1** As will be set out in further detail in the Parties’ response to the Provisional Findings, the Parties fundamentally disagree with the CMA’s provisional findings with respect to the supply of online groceries, and remain of the view that online delivered and in-store groceries compete in the same market and that a remedy to address SLCs specifically concerning online groceries is entirely unwarranted. In particular, the CMA has failed to recognise the dynamic and fast evolving nature of online delivered groceries which features a wide range of disruptive competitors, as evidenced by the recent announcement of the M&S and Ocado joint venture which will enable M&S to enter online grocery delivery and shows that it is not correct that there are high barriers to begin providing this service or that somehow the provision of online grocery is not an attractive business for competitors, both current and future.³¹
- 6.2** However, if the CMA were to conclude in its final report that online delivered groceries constitute a separate product market, and considers that the Proposed Merger will give rise to SLCs, the Parties submit that the CMA should use its discretion not to require remedies.
- 6.3** The Act provides that the CMA may determine that no action is required to remedy an identified SLC. Section 36(2) states that the CMA “*shall...decide...whether action should be*

³⁰ *Somerfield/Wm Morrison*, Final Report, paragraph 11.20.

³¹ Further discussion regarding this joint venture will be set out in the Parties’ forthcoming response to the Provisional Findings.

taken by it under section 41(2) for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned or any adverse effect which may be expected to result from, the substantial lessening of competition". Further in section 36(2)(c) the Act states the CMA is to decide "...if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented".

6.4 This is reflected in the CMA's Remedies Guidance at paragraph 1.12 in which the CMA recognises that "[i]n exceptional circumstances, even the least costly but effective remedy might be expected to incur costs that are disproportionate to the scale of the SLC and its adverse effects... In these exceptional circumstances, the [CMA] would not pursue the remedy in question."³² Further, in considering the RCBs that will be foregone due to the implementation of a particular remedy the CMA may "decide to implement a remedy other than prohibition or, in rare cases, it may decide that no remedy is appropriate".³³

6.5 In the context of the above, the CMA must consider whether the divestiture of physical stores or alternative measures to remedy the handful of Revised Online SLCs (once a 5% GUPPI threshold is applied and the margin corrected) is justifiable and proportionate, in light of the identified harm. The Parties submit that the divestiture of a bricks and mortar store, or one of the Parties' brands, to solve an online grocery SLC would be disproportionate since:

6.5.1 Online delivered grocery accounts for only a small percentage of total food sales ([X] % for Asda and [X] % for Sainsbury's in 2018).

6.5.2 Selling the bricks and mortar store to remedy an online-only SLC would deprive consumers of RCBs in the local grocery store market (assuming, as the CMA has stated, it is a separate market).

(i) For Sainsbury's store estate, approximately [X] in-store customers of that grocery store per week would be deprived of the lower prices that Sainsbury's and Asda will be able to offer as a result of the Proposed Merger, just to ensure that [X] customers a week would have the opportunity to purchase online grocery from a new or strengthened competitor in the area using that store.³⁴

(ii) For Asda, approximately [X] customers shopping in-store per week would be deprived of the lower prices that Sainsbury's and Asda will be able to offer as a result of the Proposed Merger, just to ensure that approximately [X] customers a week would have the opportunity to shop online grocery from a new or strengthened competitor in the area using that store.³⁵

These online customers will also not receive the lower grocery prices that Sainsbury's and Asda will be able to set as a result of the Proposed Merger (as online and in-store prices of groceries are the same).

6.5.3 Any online SLC would be short-lived due to entry and expansion. This is a dynamic market with a wide range of disruptive competitors, as seen by the recent news that Ocado will be entering into a joint venture with M&S, allowing M&S to enter the online delivered groceries market. Other grocery competitors could use technology offered

³² Also reflected in the Updated Remedies Guidance at paragraph 3.11.

³³ Remedies Guidance at 1.15, and Updated Remedies Guidance at paragraph 3.16.

³⁴ On the basis of transaction numbers per week for Sainsbury's stores with an online operation.

³⁵ On the basis of transaction numbers per the latest 52 week period for Asda. The numbers of customers shopping online reduces to [X] when considering delivery only.

by a provider like Ocado to begin supplying online, as Morrisons has done. There are widespread reports that Amazon is planning to launch Amazon-branded supermarkets in the USA and offers grocery home delivery in the USA and UK through Amazon Fresh, Prime Now and Whole Foods. It is clear that Amazon has the desire and resources to expand and grow its current grocery online sales to a full scale offering in the UK, its second largest international market.

- 6.6** Despite the above, and strictly without prejudice to the Parties' position – which they strongly maintain – that no remedy is warranted in this area, the Parties would be willing to discuss possible solutions to any residual concerns with the CMA.

7 Solving fuel SLCs

- 7.1** As set out in section 4 above, for the purposes of this response, and without prejudice to the Parties' response to the Provisional Findings, the Parties propose structural divestments to remedy the Revised PFS SLCs.

Enhanced divestment remedy

- 7.2** The Parties will divest PFS sites, such that each Revised PFS SLC area no longer meets a conservative threshold for concern. The Parties note that this will clearly and comprehensively address the Revised PFS SLCs. In previous cases,³⁶ such an approach has been acceptable to the CMA. CRA has assessed the Revised PFS SLCs total to be approximately 38 PFS, using diversion ratios of 40% or above, which is conservative even relative to Phase I decisional practice since the first large-scale fuel retailing merger in the Enterprise Act era (i.e. *Shell/Rontec*, 2012).³⁷
- 7.3** The Parties propose to divest the PFS alone to a fuel operator that will continue to operate the PFS to remedy concerns and ensure that the level of competition in the local area no longer meets the threshold level of concern. In addition, to solve a co-located fuel SLC and a grocery SLC, the Parties would propose to divest either (i) the grocery site and the PFS site to a grocery competitor that would operate both (such as an existing supermarket PFS operator: Morrisons, Tesco or Waitrose), or (ii) the co-located supermarket and the PFS to different purchasers, depending on the preferences of the purchaser(s).
- 7.4** In order to be an effective remedy, the PFS does not need to be sold to a supermarket competitor, nor does the co-located supermarket need to be sold in conjunction with the PFS as a package. Any purchaser will have a natural incentive to operate the divestment PFS following a low price, high volume model, given the location of the site. Supermarket PFS are typically not located in the sort of "premium" (i.e. convenient) locations favoured by oil

³⁶ For example, see OFT, *Anticipated acquisition by Rontec Investments LLP of petrol forecourts, stores and other assets from Total Downstream UK plc, Total UK Limited and their affiliates*, Case No. ME/5139/11, decision of 20 October 2011; OFT, *Completed acquisition by Shell of 253 petrol stations from Consortium Rontec Investments LLP*, Case No. ME/5191/11, decision of 3 February 2012; OFT, *Anticipated acquisition by J Sainsbury plc of 18 petrol stations from Rontec Investments LLP*, Case No. ME/5407/12, decision of 7 June 2012; CMA, *Anticipated acquisition by Asda of three grocery stores and three petrol stations from Co-operative Group Limited*, Case No. ME/6466-14, decision of 28 November 2014; CMA, *Completed acquisition by Motor Fuel Limited of 228 petrol stations and other assets from Murco Petroleum Limited*, Case No. ME/6471-14, decision of 16 February 2015; CMA, *Anticipated acquisition by Motor Fuel Limited of 90 petrol stations from Shell Service Station Properties Limited, Shell UK Limited and GOGB Limited*, Case No. ME/6534/15, decision of 26 August 2015; CMA, *Anticipated acquisition by MRH (GB) Limited of 78 service stations from Esso Petroleum Company Limited*, Case No. ME/6563/15, decision of 19 January 2016; CMA, *Completed acquisition by CD&R Fund IX of MRH (GB) Limited*, Case No. ME/6750/18, decision of 31 August 2018.

³⁷ In *Shell/Rontec*, there were 68 overlap areas and a diversion ratio of 40% was used as the screening threshold. Areas below that threshold were automatically cleared, and areas above investigated further. Ultimately, the OFT only found SLCs in areas with diversion ratios above 50%.

majors and independent PFS operators.³⁸ Accordingly, any purchaser will be incentivised to price lower than it would at one of its non-supermarket locations. Further, for some fuel operators this will fit the business model they generally operate, being focused on high volume/low price across all sites.

- 7.5** To the extent there are any residual concerns about whether a particular PFS purchaser would have a sufficient incentive to price as low as an owner of the entire site (PFS and supermarket) based on their business model, and bearing in mind the benefit from the “halo effect” of fuel sales on grocery sales³⁹, the Parties are willing, if required by the CMA, to replicate the effect of the halo contractually by a simple mechanism of a flat pence per litre payment to the new PFS owner. This would see the purchaser of the PFS acquire “virtual ownership” of the profit streams associated with the average halo, as if it owned the co-located supermarket store. Provided the level of the payment is set equivalent to the average value of the halo per litre, a purchaser of the PFS alone would have the same incentive to set low prices to obtain high volumes as an owner of the entire site.
- 7.6** The available evidence indicates an appropriate payment of around [X] to [X] pence per litre would be an appropriate incentive in addition to the factors listed in paragraph 7.4 above to ensure that divested PFS sites retain their current incentives to select low price/high volume outcomes. The Parties are prepared to ensure this “virtual ownership” by providing a [X] pence contribution of “grocery halo” to the PFS purchaser for every litre of fuel sold at the PFS for the duration of the site lease or for a period of [X] years if the freehold is sold. This will unequivocally restore the rivalry that the CMA provisionally considers will be lost in the identified local areas.
- 7.7** Each PFS would be sold to a purchaser that meets the CMA’s suitability criteria under the Remedies Guidance and Updated Remedies Guidance. The Parties will divest PFS sites, such that each Revised PFS SLC area no longer meets the CMA’s ultimate threshold for concern.

Effectiveness of the package

- 7.8** A divestiture package of this nature, including the enhanced structural remedy via the incentive mechanism, would meet each of the CMA’s criteria for effectiveness:
- 7.8.1** Divestiture of each PFS to a suitably qualified purchaser will restore the process of rivalry that the CMA considers may be lost as a result of the Proposed Merger (assessed on a conservative basis). The incentive mechanism effectively transfers the benefit of the grocery “halo effect” derived from operating both grocery stores and a PFS on a site to the purchaser of the PFS on a lasting basis. Purchasers would be incentivised to keep prices low and volumes high through the same two mechanisms (less convenient locations and grocery halo benefits) that incentivise other supermarket PFS operators today. This will also assist the structural remedy in replicating pre-merger competition.
- 7.8.2** Enhanced divestments will comprehensively and effectively remedy each Revised PFS SLC because each area will, as a result of the divestment, be below the threshold for identifying an SLC and would thus be “cleared” on a substantive review. Further, as a structural remedy, divestment will address the SLCs on a permanent

³⁸ See Merger Notice, paragraphs 871 – 873.

³⁹ The “halo effect” being that higher fuel sales are believed to lead to additional sales of in-store product lines, as some fuel customers combine purchases of fuel with purchases of items in the co-located grocery store, as identified by the CMA in its Provisional Findings, for example at paragraph 14.74.

basis, with the incentive mechanism in place for the length of the long-term lease or sub-lease, or for a period of [X] years if the sale of a freehold interest has occurred.⁴⁰ The Parties would emphasise that this timeframe (i.e. [X] years) is likely beyond the horizon of the SLC, given the expected significant reduction in fuel usage beyond the next decade.⁴¹

7.8.3 Divestments of PFS can be effected quickly (within the standard six-month timeframe allocated for divestiture remedies) and, on transition of the PFS, will act immediately to address the fuel SLCs ultimately identified. The incentive mechanism will be self-executing under the contractual documents for the divestment and compliance with it enforced by the buyer of the site.

7.8.4 Finally, the Parties are of the view that the remedy has an acceptable risk profile,⁴² and are confident that the enhanced divestments will work efficiently and address all outcomes of the fuel SLCs. The Parties' advisers have done thorough calculations to ensure that the incentive mechanism is set at an appropriate level. The Parties have a strong incentive to ensure that the incentive mechanism works in practice in order to maintain footfall to their associated grocery stores.

If a PFS needs to be sold, there is no need to sell the accompanying store

7.9 The Parties submit that a co-located supermarket store does not need to be sold to remedy an SLC in relation to fuel.

7.10 First, when defining the scope of a divestiture package, the CMA's starting point is sale of one of the overlapping businesses, which generally represents a straightforward remedy.⁴³ The CMA will "*seek to identify the smallest viable, stand-alone business that can compete successfully on an ongoing basis and that includes all the relevant operations pertinent to the area of competitive overlap*".⁴⁴ The Parties' individual fuel businesses (i.e. each PFS site) constitute the smallest viable stand-alone business able to compete successfully on an ongoing basis and it is the overlap of the individual fuel businesses which gives rise to an SLC in fuel. Selling an entire PFS site, including any associated kiosk, the transfer of staff, etc., puts the purchaser in the same position with respect to its fuel operations as the Parties prior to divestment. The CC has previously recognised that is not necessary to sell ancillary

⁴⁰ The Parties note that it may not be practicable (or possible) in some cases to assign the PFS lease if the PFS and supermarket are on the same lease. The Parties will look to provide a long-term sub-lease agreement to the maximum extent allowable (i.e. they cannot sub-lease beyond the term of their own lease). Separation of the freehold would not be expected to be problematic, provided access rights to the PFS are provided for. The CMA has previously accepted the sale of a freehold interest or, at the CMA's discretion, the grant of a long-term lease (25 years) or assignment or sub-let of a leasehold interest. See [UIL acceptance decision in MFG/MRH](#) (9 November 2018), paragraph 20. The CMA accepted that "*The divestment will occur by way of a sale of the freehold or, subject to the CMA's approval, the grant of a leasehold title (which may be subject to a break clause at 15 years exercisable at the option of the purchaser) (where either MFG or MHR holds the freehold interest in the site), or by way of an assignment of a leasehold interest.*"

⁴¹ As described in the Merger Notice, the UK fuel retailing industry is increasingly being affected by environmental concerns and the move away from fossil fuels. Following the recent concerns about diesel emissions, the UK Government has imposed a diesel car tax, in an effort to dissuade customers from using diesel vehicles, and a number of car manufacturers have announced that they will no longer sell diesel cars in the UK. Further, the Government is investing in electric vehicles in an effort to address its commitments under the Climate Change Act 2008 and has pledged to ban the sale of both petrol and diesel vehicles by 2040. These developments will inevitably result in significant changes to the competitive landscape for the supply of fuel in the UK in the medium term.

⁴² Remedies Guidance, paragraph 1.8(d).

⁴³ Remedies Guidance, paragraph 3.6.

⁴⁴ Remedies Guidance, paragraph 3.7.

assets (which do not in themselves give rise to an SLC), provided the divestiture package is attractive to purchasers.⁴⁵

- 7.11** Apart from the supermarket fuel retailers, PFS are run as stand-alone businesses by most other competitors in the market for fuel retailing. For example, oil majors such as Shell, BP and Esso, and independent forecourt operator groups such as MFG, Applegreen, Rontec and the EG Group, operate their PFS as stand-alone businesses (without any uplift from sales to a co-located supermarket). All of these players are focused on fuel and willing to invest in sites. Many of these players also generate revenue from backcourt operations, such as an attached food-to-go, store or kiosk.⁴⁶ The Parties would be willing to include both the forecourt and backcourt operations in any PFS divestment.
- 7.12** Selling the PFS in an area where the CMA has identified an SLC is an appropriate remedy, and requiring the divestment of additional assets, such as the accompanying grocery store, would come at manifestly disproportionate cost, not just to the Parties but also ultimately, to customers who will not benefit from the price investments flowing from the Proposed Merger as a result of the forced divestment.
- 7.13** This enhanced structural divestment remedy, which the Parties are willing to offer if required, is in line with CMA Guidance which provides that one of the circumstances in which the CMA will select behavioural remedies as the primary source of remedial action is where *“divestiture and/or prohibition is not feasible, or the relevant costs of any feasible structural remedy far exceed the scale of the adverse effects of the SLC”*.⁴⁷ In the present case, where the divestiture of the supermarket would be disproportionate and the contractual element of the remedy would simply be a supplement to the structural divestment of the PFS (and in particular would not require any form of regulatory oversight), the Parties consider that there can be no concerns about the acceptability of such an approach in principle.
- 7.14** Finally, requiring the divestment package for fuel SLCs to include the co-located supermarket store would be disproportionate and involve unacceptably sacrificing the significant RCBs identified in relation to the grocery aspects of the Proposed Merger. The Act at section 30(1)(a)(i) explicitly provides that RCBs to customers in another market (in this case, in-store grocery) can be taken account of when considering remedies for the market in which the SLC arises (in this case, fuel). Such a requirement would deprive the customers of the supermarket store (at which no SLC arises) from directly benefiting from the pass-through of those cost savings (and the more supermarket stores that are sold to address fuel SLCs, the greater the level of grocery RCBs sacrificed as a whole). Approximately [redacted] Asda and [redacted] Sainsbury's⁴⁸ customers a week of each supermarket would lose out on the lower prices, better quality and better shopping experience that will be able to be offered by Sainsbury's and Asda as a result of the Proposed Merger, in order for approximately [redacted] Asda and [redacted] Sainsbury's fuel customers to be offered fuel via a different competitor.⁴⁹ Ensuring customers at the PFS retain competitive prices can be achieved via

⁴⁵ For example, in *Cineworld/City Screen* (2015) the CC recognised that one of Cineworld's cinemas, in an area identified as giving rise to an SLC, contained a café which did not have to be sold as part of the cinema. In its guidance on an appropriate remedy the CC advised that “if the parties decide to sell Picturehouse Bury St Edmunds, potential purchasers should be given the option (but not be required) to buy the café to ensure that the cinema is attractive”. In this case the café was inside the cinema complex, as opposed to PFS and supermarkets which, while co-located, are easily separable. Further, there should be no concerns in the present case regarding the attractiveness of the assets.

⁴⁶ <https://www.standard.co.uk/business/retail-s-bright-spot-how-forecourt-stores-are-fuelling-profits-a3856621.html>.

⁴⁷ Updated Remedies Guidance, paragraph 3.48. See also Remedies Guidance at paragraph 7.2.

⁴⁸ Based on Sainsbury's customers of supermarkets with a PFS.

⁴⁹ On the basis of the latest 52 week period.

sale of the PFS alone, without depriving the associated grocery store customers of the benefits of the Proposed Merger.

- 7.15** The enhanced structural divestment of the PFS alone (with the contractual incentive mechanism) is a more proportionate remedy than the sale of the PFS plus a grocery store, as it preserves RCBs that will flow to customers in the grocery market while resolving the SLC in the fuel market.

8 Purchaser suitability criteria

No need to deviate from the standard criteria

- 8.1** The standard purchaser approval criteria as specified in the Remedies Guidance already require that a purchaser has access to appropriate financial resources, expertise and assets to enable the divested business to be an effective competitor in the market.
- 8.2** In *Somerfield/Wm Morrison*, the CC expressly said that “we also believe it would be appropriate to consider purchasers who are not currently within that competitor set, because they do not currently operate within these geographical markets, but who could demonstrate that they can offer PQRS comparable to those previously available in these stores. This would include regional operators that currently do not operate in these particular areas, or new entrants that could demonstrate that they would be able to compete effectively with a comparable offer.”⁵⁰
- 8.3** Thus, the CMA’s own assessment in previous cases recognises that retail operators of varying levels of “scale”, including regional operators and new entrants, are effective competitors. Each of these, and any retail operator of equivalent scale, should be prima facie considered as viable potential purchasers.
- 8.4** With regard to fuel, as set out above, PFS can be operated profitably as single sites (e.g. where run by independent dealers) or in small groups. Apart from the supermarket fuel retailers, PFS are run as stand-alone businesses by most other competitors in the market for fuel retailing. For example, oil majors such as Shell, BP and Esso, and independent forecourt operator groups such as MFG and the EG Group, operate their PFS as stand-alone businesses. Divesting the necessary assets in connection with each individual PFS will allow an acquirer to operate that site as a stand-alone business.

New entrants are acceptable purchasers

- 8.5** The Parties submit that new market entrants would be suitable purchasers and fulfil the CMA’s purchaser approval criteria. In past cases where private equity buyers and new entrants have been potential purchasers, the CMA has reviewed their suitability on a case-by-case basis, considering whether the proposed purchaser will satisfy the requirements at paragraph 3.15 of the Remedies Guidance, and thus be able to operate the divestment business so as to resolve the SLC concern and maintain competition.⁵¹ The CMA should focus on whether a suitable purchaser has the resources and management expertise to run the divested business, rather than on the identity of the purchaser.⁵²

⁵⁰ *Somerfield/Wm Morrison*, Final Report, September 2005, paragraph 11.26.

⁵¹ See, for example, *Acadia Healthcare Company/Priority Group* (2016), where two private equity firms were considered suitable purchasers of the divestment business, Notice of Consultation dated 7 October 2016, paragraph 23 et seq.

⁵² See, for example, the views of third parties in *Cygnat Heath Care/Cambian Adult Services*, Final Report, 16 October 2017, paragraph 14.92.

Other retailers, including the discounters, are acceptable purchasers

- 8.6** As the Parties have set out in detail in their previous submissions, the discounters have grown significantly in recent years in both size and range of products and exert a strong constraint on the Parties. Discounters have now been consistently included in CMA assessments (e.g. *Co-op/Nisa*; *Tesco/Booker* and this present case) and submissions from the Parties show that discounter stores have a bigger impact on their sales than the medium stores of traditional retailers.⁵³
- 8.7** The CMA acknowledges in the Provisional Findings that “*one of the major developments in the groceries sector in recent years has been the growth of the discounters (i.e. Aldi and Lidl)*”.⁵⁴ The CMA also recognises that Aldi and Lidl have also “*invested in product quality and range in recent years with Aldi’s ‘Specially Selected’ premium range now attracting sales of over £1 billion annually and over 30% of its range having been reformulated to further improve product quality*” and that it has “*received some evidence that, in the past decade or so, the perceptions of Aldi and Lidl have changed, particularly with regard to consumers’ views on the quality of their products, which is perceived to have improved and to be seen as now broadly comparable to some of the traditional grocery retailers*”.
- 8.8** Aldi and Lidl continue to expand their operations in the UK and opened 65 and 55 new stores respectively during 2018. They each have a proven track record and have built scale consistently, moving from being niche players when they entered the UK market to mainstream rivals of the Parties today.⁵⁵

9 The divestiture process

- 9.1** The Parties, along with their professional advisers, have been giving considerable thought to how to structure the divestiture process for the Proposed Remedy Package and are confident that they can complete the sale process effectively and efficiently.

The divestiture period

- 9.2** The Parties submit that the CMA should not impose any specified divestiture period. The Parties have already received expressions of interest for potential divestment stores and PFS and have every incentive to complete the divestiture process as quickly as possible in order to realise the significant synergies they have identified. This, combined with the effort that the Parties and their advisers have put into structuring the sales process, means that there is no reason why it could not be completed rapidly. In addition, the inclusion of a short divestiture period could result in creating an incentive for potential bidders to delay negotiations in an attempt to game the CMA process.
- 9.3** In any event, the period for achieving the divestitures should be no shorter than six months from the date of the CMA’s final report, the standard maximum period as provided in the Remedies Guidance.⁵⁶

⁵³ Aldi and Lidl have experience in operating fuel and online in other markets, such as Italy and Germany.

⁵⁴ Provisional Findings, paragraph 4.8.

⁵⁵ The Parties submit that the position has moved on considerably since the CC’s findings in *Somerfield/Wm Morrison*, that the discounters would not generally present a suitable purchaser of the divestment assets, but would still be considered if they could “*demonstrate that they can offer PQRS comparable to those previously available in these stores*” (*Somerfield/Wm Morrison*, Final Report, September 2005, paragraph 11.26). As such the CC advised that: “*should Somerfield demonstrate to the CC after a stipulated period of time that there is no interest in acquiring any store from any of the relevant competitors, it would be allowed to market that store more widely (including, for example, to the LADs)*” (*Somerfield/Wm Morrison*, Final Report, September 2005, paragraph 11.28).

⁵⁶ Remedies Guidance, paragraph 3.24.

Up-front buyer requirement

- 9.4** The Parties do not contest the CMA's view that the Parties must secure up-front buyers for the Proposed Remedy Package before the Proposed Merger can close. Indeed, securing up-front buyers for the divested stores and PFS is a key reason why prohibition of the Proposed Merger is not necessary and would be disproportionate. The CMA can have no credible concerns, if the Parties secure up-front purchasers for the divestment package, that the Parties will not be able to divest the required stores and PFS.
- 9.5** However, the CMA has no reason to depart from its ordinary practice of allowing the Proposed Merger to complete after a purchaser becomes contractually committed by signing a binding agreement.
- 9.6** The Remedies Guidance provides that the CMA may require an up-front buyer to complete the acquisition before the merger may proceed only in the limited circumstances where the CMA considers that: (i) the competitive capability of the divestiture package may deteriorate pending the divestiture (i.e. asset risk); or (ii) completion of the divestiture may be prolonged.⁵⁷ The Parties do not consider these to be material risks in relation to the proposed divestitures.
- 9.7** There is no risk of any of the divestment stores or PFS being neglected or run down by the Parties pre-completion. The Parties will continue to operate all stores and PFS in the ordinary course of business pending conclusion of the divestment process (subject only to the limited period of closure while the store is physically transitioned from one brand to another). If the Parties were to neglect any of their stores or PFS during this period, they would damage their own brands, which would clearly be counterproductive. Both Parties have previously been involved in numerous store swap/disposal packages while continuing to run the rest of their store estates and have a strong track record of maintaining high standards up to and including the day of closure.
- 9.8** In any event, the Parties are incentivised to continue to invest in the stores and PFS in order to maximise the proceeds from sale, and, as discussed above, the Parties and their advisers have designed the sales process with a view to creating packages of stores and PFS to maximise competitive tension amongst bidders. Any deterioration of the underlying assets would undermine this process. However, the Parties would be willing to address any residual concerns that the CMA may have in this regard through giving suitable undertakings regarding the maintenance of the stores and PFS.
- 9.9** Further, the Parties do not envisage any circumstances where the completion of the divestiture would be prolonged. In fact, the Parties have every incentive to complete the divestiture as quickly as possible so that they can focus on realising the synergies and customer benefits expected from the Proposed Merger.
- 9.10** The Parties are not aware of any previous retail cases in the UK where completion of the divestiture package has been required prior to completion of the primary transaction. To impose such a requirement on the Parties in this case would be unprecedented and disproportionate.

Trustees

- 9.11** The Parties stand ready to provide regular reporting information to the CMA to provide any assurance required that the divestment stores and PFS continue to be operated in the

⁵⁷ Remedies Guidance, paragraph 3.19.

ordinary course and that the businesses continue to be held separate pending the conclusion of the divestiture process. Accordingly, a monitoring trustee would not appear to be required. However, the Parties do not intend to raise a formal objection should a monitoring trustee be proposed.

- 9.12** Further, the Parties submit that there is also no need for the CMA to appoint a divestiture trustee because they do not anticipate any difficulty in attracting interest from a number of suitable potential purchasers. The Parties have instructed their bankers to run the sales process and expressions of interest on potential divestment stores and PFS have already been received. However, in the event that the CMA imposes a requirement for a divestiture trustee, one should only be required should the Parties fail to achieve the disposal of any part of the Proposed Remedy Package by the end of the divestiture period.

10 Relevant customer benefits

The nature of RCBs expected from the Proposed Merger, including their scale and likelihood

- 10.1** The Parties anticipate that the Proposed Merger will generate transformational levels of variable and fixed cost savings. [A consultant] has estimated that the Proposed Merger will generate £1.6 billion of synergies. As explained in the Parties' previous submissions to the CMA, the Parties believe that the synergies totals submitted to the CMA are conservative and other unquantified synergies will also arise as a result of the Proposed Merger. To demonstrate their confidence in the achievement of these synergies the Parties are prepared to offer a number of public commitments alongside the Proposed Remedy Package, to demonstrate the benefit to customers as a result of the Proposed Merger.

Price Commitments

- 10.2** As set out in section 4 above, the Parties will commit to investing £1 billion annually in lower prices across Asda and Sainsbury's by the third year following completion of the Proposed Merger. To demonstrate that the Parties are confident in this commitment, £300 million of annual price investment will be implemented as soon as practicable in the first year post-completion, prior to the synergies being realised. This will lower the price of everyday grocery items for all Sainsbury's and Asda customers in store and online.

Sainsbury's Fuel Margin Cap

- 10.3** The Proposed Merger does not involve any departure from the current pricing strategy each Party has for the sale of fuel. It is widely recognised that Asda has a long heritage of offering low fuel prices and its customers value this position. Therefore, Asda's current fuel pricing policy will not change as a result of the Proposed Merger (noting that any SLCs reasonably identified will be resolved through the enhanced divestments set out above). In order to demonstrate their confidence in the synergies that will arise from the Proposed Merger in relation to fuel (as previously explained to the CMA)⁵⁸ the Parties are willing to commit to a cap on the gross margin on fuel sold under the Sainsbury's banner, to confirm that customers will benefit as a result of the Proposed Merger. Sainsbury's will commit to sell fuel at a price

⁵⁸ As the Parties have outlined to the CMA, the Proposed Merger is expected to lead to significant savings from aligning prices on the commercial aspects where fuel is being sourced by both Parties from the same or nearby terminals ([§]), and reducing delivery costs [§]. Additional savings could also be achieved by [§]. The Parties estimate total efficiencies in relation to fuel operations to amount to £[§], and will explain why these synergies should be taken into account by the CMA in the forthcoming response to the Provisional Findings.

such that no Sainsbury's site would make gross margin of more than 3.5 pence per litre on fuel for a period of 5 years post-merger.

- 10.4** Given UK Government initiatives on green energy and reducing harmful emissions through policies such as reducing the use of diesel engines the Parties consider that it would be proportionate for the Sainsbury's Fuel Margin Cap to be reviewed after five years of operation.⁵⁹
- 10.5** Compliance with this cap would be substantiated by an independent third party, or industry body such as Fairfuel, AA or RAC who already closely monitor fuel prices, or another independent third party. The commitment can be substantiated easily, as Sainsbury's can produce weekly cost price reports.
- 10.6** This commitment would have the effect of ensuring that Asda and Sainsbury's, in addition to restoring the process of rivalry through structural divestments, will lower prices for customers in many areas not impacted by the Proposed Merger.⁶⁰ The Parties are able to make this commitment only because of the significant cost savings that will be able to be made as a result of the Proposed Merger, and thus directly benefit customers through overall lower prices and a commitment to continuing to offer low-priced fuel nationwide from Asda and Sainsbury's. The Parties expect that this would have the further customer benefit of enhancing competitive rivalry in fuel retailing across the UK.

Prohibition or divestiture as framed by the CMA would deprive customers of these RCBs

- 10.7** Under paragraph 1.15 of the Remedies Guidance, it is stated that: "*The [CMA] will normally take relevant customer benefits into account, as permitted by the Act, once it has decided on the existence of an SLC by considering the extent to which alternative remedies may preserve such benefits. In essence, relevant customer benefits that will be foregone due to the implementation of a particular remedy may be considered a cost of that remedy by the [CMA]. The [CMA] may modify a remedy to ensure retention of a relevant customer benefit or it may change its remedy selection, for instance it may decide to implement a remedy other than prohibition or, in rare cases, it may decide that no remedy is appropriate.*"
- 10.8** At Phase II, the CMA will normally take RCBs into account by considering the extent to which alternative remedies may preserve such benefits. The Parties have provided convincing evidence regarding the nature and scale of RCBs, substantiated by two independent consultants, to clearly demonstrate that the quantified synergies fall within the Act's definition of such benefits.⁶¹
- 10.9** The Parties have sought to structure the Proposed Remedy Package in a proportionate manner and so as to preserve, as far as possible, the RCBs within the meaning of section 36(4) of the Act in accordance with the CMA's statutory obligations. Further, as a result of

⁵⁹ It would be unnecessary and disproportionate for the Parties to commit to this margin cap for a longer period given the uncertainties regarding the future of petrol and diesel vehicles in the UK and the rise in popularity of electric vehicles. As described in the Merger Notice, the UK fuel retailing industry is increasingly being affected by environmental concerns and the move away from fossil fuels.

⁶⁰ [§<]

⁶¹ The Act provides that a benefit is only an RCB if it accrues from the creation of the relevant merger situation concerned or may be expected to accrue within a reasonable period from the creation of that merger situation AND would be unlikely to accrue "*without the creation of that situation or a similar lessening of competition*" (section 30(2) and 30(3) of the Act). Moreover, to qualify as an RCB, the prospective cost reductions must be expected to result in lower prices (or better quality, service, choice or innovation) than if the merger did not take place (Updated Remedies Guidance, paragraph 3.22).

the efficiencies that will be achieved from the Proposed Merger, the Parties are able to offer the additional Public Commitments that will demonstrate the direct, instant and ongoing benefit to consumers from the Proposed Merger. These benefits would not be available to consumers were the Proposed Merger to be prohibited, or were divestment to occur on the terms outlined by the CMA in the Remedies Notice. The CMA's suggested package is not proportionate and would see much of the efficiencies underpinning the motivation for the Proposed Merger undermined and the Proposed Merger effectively prohibited.