Department for Business and Trade Consultation, Smarter regulation: strengthening the economic regulation of the energy, water and telecoms sectors - response from the Competition and Markets Authority

Background & Introduction

1. The CMA is the UK's principal competition and consumer authority. It is an independent non-ministerial government department and its responsibilities include carrying out investigations into mergers and markets and enforcing competition and consumer law. The CMA helps people, businesses and the UK economy by promoting competitive markets and tackling unfair behaviour.

2. The CMA has a cross-economy, UK-wide role and (unlike Ofgem, Ofcom and Ofwat) is not focused on regulating any particular sectors. The CMA does not have multiple statutory duties or objectives that we are required to prioritise or balance against each other. The CMA benefits from a single clear, statutory duty: "to promote competition, both within and outside the United Kingdom, for the benefit of consumers".

3. While the CMA has a wide range of statutory functions that it delivers in line with the relevant legislation, this single statutory duty underpins all of the CMA's work, with only one exception.[1] It provides a clarity and consistency of purpose that enables us to deliver effectively across all our different functions, focused on outcomes.

4. The CMA supports the underlying objectives of DBT's consultation 'Smarter regulation: strengthening the economic regulation of the energy, water and telecoms sectors' to ensure that regulatory frameworks are supporting good outcomes for the economy, consumers and the environment.

5. The CMA particularly welcomes DBT's focus on promoting effective competition. Effective competition happens when businesses compete to win customers by offering them a better deal. When firms compete effectively with

[1] The only exception is the CMA's internal market function, where Parliament gave the CMA a separate statutory objective of supporting, through the application of economic and other expertise, the effective operation of the UK internal market.

each other, they cannot raise prices, or cut quality and service, without losing business. If competition is weak or ineffective, firms do not face the same pressures to keep prices down; to keep quality up; to operate efficiently; or to innovate. This comes at a cost to consumers, other businesses and the wider economy:

(a) Weak competition harms consumers: the cost of weak competition is borne by consumers in the form of higher prices, lower quality and less innovation. This raises the cost of living,[2] and it can hit the poorest households hardest.[3] With fewer suppliers to choose from, and less innovation, consumers also suffer from reduced choice.

(b) Weak competition can harm businesses: just as consumers pay more when competition is weak, businesses pay more than they should to their suppliers. And when markets are dominated by a small number of powerful firms, they can use their position to prevent other businesses from entering and growing. Both of these factors lead to higher prices for customers of those businesses.

(c) Weak competition harms the economy as a whole: because firms do not face pressures to operate as efficiently as possible, the people employed by them are not as productive as they could be. Nor do they face the same pressures to innovate, in order to get ahead of their rivals. This inefficiency and lack of innovation comes at a cost to the economy, in the form of reduced job creation, weaker productivity and slower wage growth. In countries where competition is stronger, productivity and hence wage growth tends to be higher.

6. Economic regulators (including Ofgem, Ofcom and Ofwat) have an important role to play in promoting effective competition, including through protecting consumers, in the sectors they regulate. Promoting effective competition in turn helps drive productivity growth, encourage innovation and provide consumer and businesses with better deals and new goods and services.

7. The importance of competition in the UK economy for driving innovation and productivity and delivering benefits consumers is reflected in the UK Government's strategic steer to the CMA and in both the CMA's 2023-24 Annual Plan and the CMA's 2024-2025 draft Annual Plan. Both Annual Plans are focused on the CMA's purpose to help people, businesses and the UK

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[2] European Central Bank (2005), Does product market competition reduce inflation

[3] See for example, Ennis, S. et al. (2019), Inequality: A hidden cost of market power; Gans et al. (2019) Inequality and market concentration. Concentration, industry structure, and distributional impacts of this report also considers the relationship between incomes and competition.

economy by promoting competitive markets and tackling unfair behaviour to help ensure that:

(a) People can be confident they are getting great choices and fair deals;

(b) Competitive, fair-dealing businesses can innovate and thrive;

(c) The whole UK economy can grow productively and sustainably.

The CMA's response to the consultation

8. The CMA's role and functions interact with regulated sectors and regulators in a number of ways. Most relevant to this consultation are:

(a) **Concurrency:** For certain of the CMA's functions (enforcing competition and consumer law and conducting market studies), the CMA shares the power to take action in specific sectors with the relevant sector regulator (known as 'concurrency'). In these contexts, the CMA and sector regulators work in partnership, and we aim to coordinate and support each other in our work.

(b) **Regulatory appeals and redeterminations**: The CMA is responsible for reviewing certain decisions taken by other sectoral regulators. In this context, the CMA fulfils a quasi-judicial role. The CMA's hearing of regulatory appeals and redeterminations provides an important 'check and balance' function, applying an appropriately rigorous standard of review to regulators' decisions. The value in this function is in the independence and expertise of the CMA in hearing appeals of decisions taken by regulators. It should be noted that the decision-makers in regulatory appeals are members of the CMA's independent panel and not CMA officials.

9. This response focuses on the parts of the consultation most closely related to these two areas, where the CMA can bring a unique perspective and has a direct role in the landscape. Beyond this response, the CMA has been actively engaging with various governmental and parliamentary reviews of the regulatory landscape. For example, the CMA's Chair, Marcus Bokkerink, gave oral evidence in November 2023 to the House of Lords Industry and Regulators Committee's inquiry into UK regulators.[4] This covered, among other things, the CMA's approach to regulatory co-operation, performance and accountability, and engaging with businesses and consumers. The CMA also submitted written evidence to the inquiry and has set out how this written

[4] House of Lords Industry and Regulators Committee inquiry into UK regulators - Oral evidence 29 November 2023; House of Lords Industry and Regulators Committee inquiry into UK regulators - Written evidence published 13 December 2023

evidence maps to the questions in DBT's open call for evidence on Smarter regulation and the regulatory landscape consultation. The CMA has also engaged on recent UK reforms to regulatory impact assessments, and updated in July 23 its own guidance to policymakers on competition assessment which include a greater focus on innovation. Further to this response, the CMA would be happy to engage with UK Government on other specific proposals in the consultation where helpful.

10. The CMA welcomes and supports proposed reforms to the appeal regimes which, as a package, will help to both improve and simplify specific appeals processes and the overall appeals landscape. The CMA particularly supports the proposal to move the water regime from a redetermination to an appeal standard. This would increase consistency across regulated sectors, and in water would focus the role of the CMA towards its particular areas of expertise, reduce uncertainty for stakeholders, and establish a more targeted and proportionate approach to checks and balances. The CMA believes this would ultimately benefit both investors and consumers.

Consultation response to Chapter 4: Competition – Concurrency

Question 22 - Do the existing concurrency powers and arrangements deter or address anticompetitive behaviour in the regulated sectors? Please explain the reasons underpinning your response.

Overview

11. The CMA considers that '**Concurrency**' in its broader sense refers to the framework in which responsibility for the promotion of competition in the regulated sectors is shared between the sector regulators and the CMA.

12. The '**concurrent powers**' are the specific competition powers which are shared between the sector regulators and the CMA. These are:

    (a) Antitrust enforcement powers: the powers to apply the prohibitions on businesses engaging in anti-competitive agreements or on the abuse of a dominant market position (respectively, the Chapters I and II prohibitions of the Competition Act 1998).

    (b) Enterprise Act markets powers: the powers under Part 4 of the Enterprise Act 2002 to conduct market studies and, if appropriate, make a market investigation reference to the CMA.

13. There are various procedural mechanisms, set out in law, guidance and bilateral memoranda of understanding between the sector regulators and the

CMA, which underpin the sharing of concurrent powers. Collectively, these are often referred to as the '**concurrency arrangements**'.

CMA's ongoing review of concurrency

14. Although concurrency is a longstanding feature of the UK's competition regime, the Enterprise and Regulatory Reform Act 2013 introduced a series of reforms to the arrangements by which the sector regulators and the CMA use these powers. These reforms came into effect in 2014.

15. 2024 will therefore mark ten years since these enhanced concurrency arrangements were introduced. The CMA considers that this is a good opportunity to consider the objectives and performance of concurrency more broadly. The CMA therefore commenced a review of the effectiveness of the competition concurrency arrangements in August 2023, publishing a call for inputs to collect evidence and views.

16. Our review is considering the objectives and performance of concurrency, ten years on from the reforms in 2014. In broad terms, the CMA is considering the following questions:

    (a) To what extent does concurrency improve the effectiveness of the sector regulators in promoting competition in their respective sectors? As part of this, we are considering the extent to which antitrust enforcement powers and Enterprise Act markets powers help sector regulators promote competition in their sectors, as well as how concurrency impacts on sector regulators' wider regulatory functions.

    (b) To what extent does concurrency improve the effectiveness of the UK's competition regime? As part of this, we are considering the extent to which concurrency leads to stronger deterrence against breaches of competition law both across the economy and within the regulated sectors.

    (c) Are there improvements which could be made to concurrency? As part of this, we are considering whether the arrangements for cooperation between the sector regulators and the CMA on their concurrent powers could be improved.

17. The CMA's review is ongoing, and we are aiming to report on our findings in spring 2024. We look forward to sharing the views that we have received and our assessment of the effectiveness of concurrency with DBT, as well as any opportunities to make improvements.

Consultation response to Chapter 5: Appeals

Question 32. The government welcomes your views on enabling the CMA to have the additional flexibility to appoint larger groups to hear non-price control water appeals and energy appeals. What might be the downside of this approach? Do you have any evidence of alternative models, e.g. international comparators?

18. There is a requirement in the appeal regimes for energy, water (non-price control), airports and air traffic services for the CMA to appoint a group of exactly three members to hear these appeals. This contrasts with other sectors (eg water redeterminations and telecoms appeals) where the CMA has the flexibility to appoint a larger group where appropriate. Amending the legislation for these appeals would also align the approach taken with the appointment of groups in other analogous proceedings (eg Phase 2 merger inquiries or market investigations).

19. The additional flexibility on the size of the group will help ensure the appropriate balance of skills and experience within the group for the challenge of a particular appeal and the relevant statutory deadlines, and it will provide resilience. This is particularly important in the light of the scope and scale of appeals which we have come to expect, given recent experience.

20. A potential downside of this approach is a slight increase in CMA costs incurred in the appeal, as the cost of any additional panel members will need to be included. We consider that the increase will be limited since the cost of the panel members is only a small proportion of the total CMA cost of an appeal. However, in the CMA's view, this downside will be outweighed by the considerable benefits (which are set out in the preceding paragraph) and the extent of the consequent cost increase is unclear as to some extent the same work (and hours) will be spread across more panel group members.

21. The provision in the appeal regimes for energy, water (non-price control), airports and air traffic services that requires the CMA to appoint a group of exactly three members also sets out requirements for decision-making. A decision of the group is only effective if all members of the group are present when it is made and at least two members of the group are in favour of the decision. The inability of groups to be able to take decisions unless all members are available and the requirement for all members to be present (whether in person or remotely) can pose challenges in practice. Therefore, in addition to giving the CMA the flexibility to appoint a larger group, the CMA would also welcome the introduction of a provision that would enable the

group to set a quorum that would allow, where appropriate, for decisions to be taken even if not all members are available.[5]

Question 33. What are the risks to consider before giving CMA power to directly extend deadlines in energy and water appeals? What opportunities do you feel this proposal may create? Do you have evidence regarding this proposal that the government should consider?

22. We consider that granting the CMA the power to directly extend deadlines in energy and water appeals would be more consistent with the overriding objective of these regimes[6]. By giving more control to the CMA over the granting of extensions, this would allow for greater efficiency/effectiveness of the planning of the appeal by the CMA. It would also be consistent with the CMA's powers in other regimes (such as in market investigation references under the Enterprise Act 2002).

23. In practice, it is in the CMA's interest to complete an appeal as quickly as practicable given other calls on resources, so there is an incentive not to extend unnecessarily and in any event the CMA would be unlikely to extend the timetable without first inviting representations from the parties.

24. We note that the UK Government states in the consultation document that the CAT follows separate procedures for telecoms appeals which it considers work well in general. However, in telecoms appeals the CAT determines the procedure and the CMA considers that this creates a number of complications – primarily that the CMA does not have control over the timing of the case, access to documents, or clarity of the scope of the issues likely to fall to it, until potentially a couple of weeks before the start date of what may be a major appeal. This uncertainty makes appointing an appropriate Panel and CMA staff team and planning an appropriate work programme unnecessarily difficult.

25. The CMA would like to have an express right to be heard on these process issues. One way to do this would be for the CMA to be involved in the case management conference as a matter of course and for its views on appropriate process of the price control elements of appeal to be given due weight. For example, the CAT's guidance does not make express provision for the CMA to make submissions at the Case Management Conference on

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[5] This would be consistent with the approach to decisions that are taken by CMA groups in mergers and market investigations (as set out in Schedule 4 of the Enterprise and Regulatory Reform Act 2013).

[6] The overriding objective in the energy and water appeals regimes is set out in the relevant Rules and is to enable the CMA to dispose of appeals fairly, efficiently and at proportionate cost within the time periods prescribed by the relevant Acts.

the price control elements of the process and instead of requiring parties to serve pleadings raising potential price control issues on the CMA, the guidance merely states that it is likely to be expedient to do so. We consider that these issues could be addressed by appropriate changes to the CAT Rules and Guidance.

Question 34. In what other ways can the consumer voice be represented during energy, water and telecoms appeals?

26. We recognise the importance of ensuring that the consumer voice is heard in the appeal process, and we welcome the UK Government's proposal to explore amending the statutory basis for cost recovery to enable the CMA and the CAT to recover reasonable costs from the losing party incurred by an intervener when they acted on a 'consumer interest' basis as this may encourage more consumer bodies to bring appeals.

27. It should though be noted that there are ways in which the consumer voice is brought into the process, even under the current regime. The CMA is required, in most of the appeal regimes, to have regard to the regulator's duties and objectives to the same extent as is required of the regulator. As the regulators are typically subject to objectives or duties to protect the interests of consumers, the CMA has to have regard to such objectives and duties in determining whether the regulator erred.

28. Furthermore, the CMA has a wide discretion as to how to determine the appeal process and can use that flexibility to allow consumer bodies the opportunity to be heard. Indeed, in regimes such as energy appeals, consumer bodies (Citizens Advice, Consumer Scotland and the Consumer Council for Northern Ireland) have standing provided that they are acting in the capacity of representing consumers whose interests are materially affected by the decision, and in the airports regime a provider of air transport services whose interests are materially affected by the decision can appeal. Even if they do not appeal, these consumer bodies often seek to intervene in appeals.

29. However, in water redeterminations, consumer bodies do not have standing to appeal. While the CMA nonetheless seeks to ensure that consumer bodies are given the opportunity to make representations, the voice of the consumer could be brought into the process to a greater extent if the water regime and other regimes that do not currently give consumer bodies or customers standing to appeal or to intervene were amended to bring them into line with energy appeals.

30. A further way to bring the consumer voice into appeals to a greater extent would be to address the difficulties that consumer bodies often face in exercising their rights in practice. This is part of a broader challenge in economic regulation, that the quality of evidence from consumer bodies may be affected by their lack of resource and access to experts.

Question 35. Are there any concerns or opportunities you foresee in allowing interveners, who have acted on behalf of consumers interest, to recover reasonable costs incurred alongside the body hearing the appeals costs? How may this impact case and legal practice in this sector? What would be useful to include in the guidance for the appeals body to deliver this mechanism?

31. The statutory basis for costs recovery would need to be amended such that the CMA had a duty to grant permission to an intervener on a 'consumer interest' basis, and in that scenario, such an intervener's reasonable costs would be recovered by the CMA along with its own costs.

32. We note the UK Government's observation that making this amendment may incentivise more interveners or lead to an increased volume of detailed evidence parties need to review, meaning it may take longer to process the appeal, with more resources required. The CMA acknowledges this risk and considers that it might need to produce guidance about the eligibility criteria and to have discretion to limit the number of consumer interest interveners and to manage the submission of evidence (such as by setting page limits). It might also need to set conditions, such as a specific upper limit on costs, to the granting of permission. Such measures would seek to avoid imposing too heavy a burden on the parties as well as risks for the CMA's process and to avoid cost escalation disproportionate to the value added by the interventions.

Question 36. What unintended consequences or risks should the government be aware of when considering making this amendment to code modification appeals [to align them with energy licence modifications, giving discretion to the CMA to apportion its costs as it considers appropriate]?

33. The CMA welcomes the UK Government's proposals to give the CMA discretion to apportion its costs as it considers appropriate in code modification appeals, aligning the provisions in paragraph 13 of Schedule 22 to the Energy Act 2004 with the corresponding provisions in paragraph 12 of Schedule 5A to the Electricity Act 1989. We do not consider there to be any unintended consequences or risks in making this amendment to code modification appeals.

34. The CMA is engaging with the team in DESNZ who are looking in more detail at reform of the code modification regime and we look forward to the code

modification appeal regime being reformed in due course. For example, we have particular concerns with the statutory deadline for code modification appeals of two months. Recent cases have involved issues of a technical and legal nature that have not been issues which were well-suited to being heard in so short a timeframe.

Question 37. What are the costs and benefits of moving the regime from a redetermination to an appeal standard? Do you have any evidence for this, for example from other regulated sectors or international examples of appeal regimes?

35. The CMA considers there are several benefits in moving the regime from a redetermination to an appeal standard:

- Increasing the degree of alignment between the different appeal processes would benefit the regulated sectors as a whole. The inconsistencies in the standard of review between appeals and redeterminations would be removed, reducing legal risk and uncertainty in the process for all.

- In particular, we consider that investors and others who are looking at UK infrastructure businesses as a whole may find that the differences in regimes increase uncertainty and make it more difficult to make judgements across sectors. Investors may be uncertain about the level of consistency between the CMA's decisions in water and energy, even on seemingly comparable measures such as the cost of capital, due to the different questions put to the CMA under the different legal frameworks. We also note that redeterminations bring greater uncertainty to stakeholders more generally, as the CMA's decisions are not bounded by the grounds of appeal.

- The scope of a redetermination creates practical difficulties for the CMA. For example, Ofwat's price controls cover several thousand pages and were produced over a period of five years. The whole of this price control was sent to the CMA to determine for four companies with distinct business plans and investment requirements in a period of six months, extendable to one year.

- One of the core reasons for having an appeal regime is to provide checks and balances against a regulator making errors in its analysis. Both an appeal and a redetermination can do this. However, the CMA's review in appeals focuses on the errors that the appellants have identified in regulators' decisions and are therefore more targeted and more consistent with the need for speed in reviewing these decisions.

Furthermore, within an appeal, matters on which the CMA has no obvious expertise can be assessed based on the quality of evidence and reasoning provided by each party, with the question being whether the regulator's decision is wrong on the specific grounds raised by the appellant, rather than the CMA being expected to take a fresh look and come to its own view in a redetermination. Some stakeholders raise concerns about the risks of cherry-picking in an appeal and the possibility that the CMA finding an error in one element of the regulatory decision may upset the regulatory balance of the overall decision. However, for reasons explained further in response to Question 38 below, the CMA considers that those risks can be reduced considerably by addressing interlinkages in the appeal process.

- By contrast, a redetermination goes further than an appeal – even where there is found to be no 'error' in the regulator's reasoning, the CMA is nonetheless required to substitute its own view if it would have reached a different decision. For example, in the CMA's PR19 water redetermination, the CMA preferred a higher cost of capital as a result of a different balancing of the issues presented. In making that determination, the CMA did not look through the appeal lens of an 'error'; the redetermination involved the CMA taking a different view from the regulator rather than merely correcting any flawed reasoning or erroneous findings. There are some stakeholders who value the role played by the CMA in holding a regulator to account in a redetermination and, as the consultation document notes, they see the water redetermination as a 'gold standard'. However, the CMA only has, as noted above, six months (extendable to one year) to redetermine a price control decision that the regulator has taken several years to make and therefore sees value in the more targeted approach of the appeal process.

- We note that redeterminations are a two-way bet (in that, as the CMA is redetermining the regulator's decision, the outcome may not necessarily favour the appellant). However, appeals have the advantage that they allow for two-way appeals by both customers and companies (and not just by the companies as is the case for water redeterminations).

- In the 2000s, when price controls were less complex, the Competition Commission (the predecessor of the CMA) had redetermination powers in all sectors except telecoms. Over the last few years there has been a general shift away from redeterminations towards appeals. There does not appear to be a good reason for maintaining different regimes. We consider that alignment between the regimes should take place and, while we acknowledge that there are arguments in favour of redeterminations,

on balance, for the reasons set out above, we consider that alignment should be achieved by bringing water into line with the other main sectors.

Question 38. What risks of making this change [ie moving from redetermination to an appeals standard in water] should the government be aware of?

36. We note that some stakeholders have in the past identified 'cherry picking' as a potential risk of moving a redetermination regime to an appeals standard. The concern is that, by considering one element of a regulator's decision in isolation, that might undermine the global 'bargain' struck by the regulator with the relevant licence holders. We consider that this risk is inherent in an appeals regime, but can be addressed to a considerable extent by considering interlinkages through the existing process, ie by recognising that in some circumstances it might be necessary to take care that overturning one aspect of a complex regulatory decision does not have knock-on consequences for other aspects of the decision that have not been appealed.

37. Furthermore, following its determination in an appeal, one of the CMA's powers is to remit the matter back to the relevant regulator for reconsideration and determination in accordance with any directions given by the CMA, which means that the CMA can direct the regulator to consider the issue that is the subject of the appeal in the round when implementing the remedies ordered by the CMA.

38. We consider that any disadvantages of the appeal regime are outweighed by the advantages of moving away from redeterminations.

Competition and Markets Authority
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