Linklaters

# Draft guidance on the CMA's investigation procedures in Competition Act 1998 cases (CMA8), draft guidance on the CMA's mergers jurisdiction and procedure (CMA2) and draft statutory instrument on The Competition Act 1998 (Determination of Turnover for Penalties) Regulations 2024

## Linklaters' Response

## 10 September 2024

## 1 Introduction

(1) We are pleased to respond to the Competition and Markets Authority's ("**CMA**") consultation on the draft revised guidance on the CMA's mergers jurisdiction and procedure ("**Draft CMA2**") and the draft revised guidance on the CMA's investigation procedures in Competition Act 1998 cases ("**Draft CMA8**") (together, "**Draft Guidance**"), as well as the draft statutory instrument for the Determination of Turnover for Penalties Regulations ("**Draft Regulations**").

(2) By way of general comment, we welcome the additional clarity provided by the Draft Guidance and Draft Regulations. However, as we set out in this response, there remain some areas that we consider would benefit from greater clarity and / or detail.

(3) In this response, we comment in particular on: (1) scope of documents subject to the duty to preserve documents relevant to investigators in CMA8; (2) the scope of the UK nexus test in CMA2; (3) the extraterritorial application of requests for information in CMA2; and (4) the inclusion of free services when determining turnover for penalties in the Draft Regulations.

## 2 Draft CMA2

### 2.1 UK Nexus Test

(4) Paragraphs 4.72 to 4.90 of Draft CMA2 provide welcome clarifications regarding the application of the UK nexus threshold in the new 'hybrid test.'

(5) However, as regards the limb relating to the target carrying on 'at least part of its activities' in the UK, we are concerned that the guidance is overly broad and does not provide sufficient clarity so as to enable parties to determine the circumstances in which this limb may, or may not, be satisfied.

(6) In particular, the guidance states, as an example, that an enterprise may carry on part of its activities in the UK if 'consumers in the UK have access to the goods or services of the enterprise;'[1] Having regard to the Competition Act 1998 ("**CA98**"), pursuant to which sales restriction and market sharing arrangements may be unlawful, it would in our view be beneficial to distinguish between the active targeting of consumers in the UK (for example through advertising, tailoring products/services for consumers in the UK) and more passive access to goods or services.

(7) Similarly, the inclusion of 'any preparatory step' towards potentially supplying goods or services in the UK is overly broad. As currently drafted, it is not clear what would constitute 'preparatory' steps, and whether this wording would capture activities which take place

[1] Draft CMA2, paragraph 4.88.

entirely outside of the UK where no actual supply might eventuate (for example, feasibility assessments conducted outside the UK to determine whether to supply in the UK).

### 2.2 Extraterritorial application of formal requests for information

(8) Under the DMCC Act, the CMA can issue formal requests for information extraterritorially to persons 'carrying on business in the UK'. Examples of when this so-called 'UK connection' test is satisfied are outlined in paragraph 9.31 of Draft CMA2. While we welcome the use of examples to clarify the application of this threshold, we query the inclusion of paragraph 9.31(d), which provides that the test is satisfied where 'a person does not directly sell goods or services in the UK but provides a key input or component (e.g. software) for a good or service that is ultimately supplied in the UK.' In circumstances where a party supplies a component to another party without any influence over where the goods or services are ultimately supplied, it would seem to us questionable that that party could be said to be carrying on business in the UK.

## 3 CMA8: Duty to preserve documents

(9) Following the commencement of the Digital Markes, Competition and Consumers Act 2024 ("**DMCCA24**"), the CA98 will impose an obligation not to falsify, conceal, destroy or otherwise dispose of a document which a person knows or suspects is or would be relevant to the investigation (or cause or permit this to be done).[2] Failure to comply with this obligation, without reasonable excuse, can result in a fine.

(10) In line with this obligation, at paras 5.10 and 5.11, the Draft CMA8 sets out what types of documents the CMA will consider as subject to the preservation obligation. However, it is our view this is currently drafted too broadly, resulting in an obligation to preserve documents that would be irrelevant to an investigation. Further clarification is needed to enable industry participants to ascertain what documents they are legally required to preserve.

(11) Standard document destruction policies generally provide that data only be kept for as long as there is an administrative need, or for as long as is required to demonstrate compliance for audit purposes or to meet specific legislative requirements.[3] Such policies are crucial to ensuring businesses adequately safeguard sensitive information, prevent data breaches and comply with data protection regulations. Imposing an open-ended obligation to retain information for an indeterminate amount of time, on a vague category of documents – especially where retaining such information may be contrary to standard document destruction practices – is likely to be difficult for industry participants to comply with.

### 3.1 Documents containing background information

(12) Under para 5.10 of the Draft CMA8, the obligation to preserve documents extends to documents containing "background information". However, is not clear what types of "background information" the obligation could apply to, especially when it comes to the scope and timeframe of relevant background information. Further clarity is extremely important on this point in order to provide legal certainty, particularly where industry participants may be subject to financial penalties for even an accidental failure to retain documents.

#### 3.1.1 Scope of background information

[2] Draft CMA8 at para 5.9, and Section 25B and 40ZE(1) of the CA98.

[3] See, for example, the HMRC guidance on Archiving trade documents, updated 13 August 2024. See also the CMA's data retention policy, published 18 February 2022.

(13) Para 5.10 notes that "background information" includes "information about conditions in the market in which the suspected infringement occurred". This drafting could potentially cover an extremely broad range of documents and indeed anything relating to the product in question, which could conceivably capture almost any document.

(14) To avoid uncertainty, we suggest that CMA8 clarify that "background information" means background information about the product and geographic markets relevant to subject matter of the investigation. It would also be helpful for the CMA to further specify what kinds of background documents would be considered relevant (e.g. those which contain internal or external *analysis*) so that industry participants can more clearly ascertain what types of information are covered by the obligation.

#### 3.1.2 Timeframe for background information

(15) There should be a clear timeframe for what "background information" might be considered relevant, and this should – unless the CMA explicitly requests otherwise – be limited to the period under investigation. For example, it would not be proportionate to require industry participants to retain documents that contain background information about a market where those documents are so historic that they no longer shed any light on the product or geographic markets.

### 3.2 Documents related to areas "initially adjacent" to the investigation

(16) Para 5.11 of Draft CMA8 provides that "as a matter of good practice" a broad view of relevant documents should be taken, noting that "the scope of a CMA investigation may change over time and this may include an extension of the scope of the investigation to areas which are initially adjacent to the investigation."

(17) First, it is not clear from this drafting whether or not the CMA considers there to be an obligation to preserve documents which are outside the scope of an investigation (but which may later be in scope), or whether para 5.11 is merely a suggestion. Our view is that it would not be appropriate or proportionate to extend scope beyond areas under investigation – the legislation itself provides the touchstone in its requirement that an individual "knows or suspects" might be relevant. There can patently be no obligation to retain documents outside of these circumstances, which will always be dependent on the facts of the case.

(18) Nor is it clear what is meant by "adjacent to the investigation". This is likely to make it difficult for undertakings and their employees to understand what documents they are required to retain in order to meet their obligation. Given the high level of penalties that can be imposed, even in the cases of unintentional breach, the need for legal certainty in this respect is extremely important.

(19) Further, where the CMA makes an information request or warrant, it can only require the production of documents which are "relevant" to the investigation currently underway. For written information requests, this would be documents "relevant to the investigation at the time the request is sent out",[4] while in a dawn raid, this would be those documents which are relevant at the time the raid is carried out.

(20) Creating an obligation to retain documents "initially adjacent to" an investigation would mean undertakings would be required to retain documents they are not required to produce to the CMA in a written information request or a dawn raid. Those responsible for retaining documents would not reasonably contemplate that they would be required to retain such

[4] CMA8 at para. 6.6; Draft CMA8 at para. 6.6.

documents, and requiring they be retained is therefore contrary to the principles of legitimate expectations. Further, fining undertakings or individuals for (even accidentally) failing to retain documents which they are not required to produce to the CMA would be disproportionate.

## 4 Determination of Turnover for Penalties: Free services

(21) When read with the CMA's consultation document on the proposed turnover and control regulations ("**Consultation Document**"),[5] it is not clear whether the Draft Regulations relating to calculating turnover for penalties are intended to include services that are free to end-users in the calculation of turnover. This casts some uncertainty over how the Draft Regulations would be applied.

(22) Specifically, when describing how turnover will be estimated or determined (both for calculating penalties and in respect of SMS designation), the CMA states in the Consultation Document that:

> "The substantive approach taken in each set of regulations is that the turnover of an undertaking, group or enterprise is the sum of all amounts it derives from the provision of goods and services (broadly speaking), less any sales rebates, value added tax, and other taxes which are directly related to turnover.
>
> The policy intention is that this should include services that are free to end-users but otherwise monetised, such as digital services that make money from third-party advertising." [Emphasis added]

(23) With respect to SMS designation, this policy intention is reflected by proposed wording which would require the CMA have regard to "whether the amounts… are derived in connection with the direct or indirect supply of products…" and "whether the amounts…derived in connection with products which are used, viewed or otherwise consumed by UK users or UK customers." Considering the purpose of the legislation and the types of enterprises which might receive an SMS designation, it is not unexpected that this could include services that are free to end-users in the calculation of turnover.

(24) However, that is not the case with respect to calculating penalties under the CA98 or the Enterprise Act 2002 ("**EA02**") more generally, nor is it clear from the proposed drafting that free services would be included in the determination of turnover. Specifically, with respect to calculating penalties, the proposed change is to amend The Competition Act 1998 (Determination of Turnover for Penalties) Regulations to define turnover as:

> *"the sum of all amounts derived by the undertaking from its sale of products and provision of services, after the deduction of sales rebates, value added tax and other taxes directly related to turnover."*

(25) Similarly, the CMA proposes amending The Enterprise Act 2002 (Mergers and Market Investigations) (Determination of Control and Turnover for Penalties) Regulations 2024 to define turnover as:

> *"the sum of all amounts derived from the sale of goods and provision of services, after the deduction of sales rebates, value added tax and other taxes directly related to turnover."*

[5] DMCCA 2024 turnover and control regulations: consultation (published 30 July 2024).

(26) In both cases, the CMA proposes removing "ordinary activities" (noting in the Consultation Document that this change is merely to reflect changes in the Companies Act 2006) but otherwise no substantive changes are proposed, and certainly none which indicate that the provision of free services would be included when determining turnover (despite the CMA's statements of its policy intention in the Consultation Document). It therefore appears to us that the CMA does not propose amending the approach to determining turnover for penalties to include "free services", and that its statement about its policy intention relates to SMS designation only. To avoid any uncertainty on this point from industry participants, we ask that that the CMA clarify this point.

(27) For completeness, we note that in our view "free services" should not be included in determining turnover for penalties, as this is a move away from the bright line approach to determining turnover in penalties situations and would create significant uncertainty for industry participants. Penalty calculations which are based on turnover should be clear, understandable and easily administrable. Requiring industry participants to determine their turnover with regard to "free services" which are later monetised is likely to be incredibly difficult, especially for non-digital services and those in industries who may not be reasonably expected to keep track of such information, as will the CMA's role of adjudicating this.

**Linklaters LLP – 10 September 2024**