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COMPTROLLER AND  
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**22 MARCH 2010**

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# Review of the UK's Competition Landscape

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National Audit Office

# Review of the UK's Competition Landscape

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Amyas Morse  
Comptroller and  
Auditor General  
National Audit Office  
18 March 2010

Competitive markets are an essential component of the UK economy and are of vital importance in delivering goods and services cost-effectively to UK consumers. Where markets fail, consumers can suffer great detriment. The Office of Fair Trading estimates that, without its work on market studies, mergers, and competition enforcement, consumers would suffer some £340 million of detriment annually.

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This report can be found on the  
National Audit Office website at  
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# Summary

**1** Competitive markets are an essential component of the UK economy and are of vital importance in delivering goods and services cost-effectively to UK consumers. Where markets fail, consumers can suffer great detriment. The Office of Fair Trading estimates that, without its work on market studies, mergers, and competition enforcement, consumers would suffer some £340 million of detriment annually.<sup>1</sup> The Competition Commission has calculated a consumer benefit of £295 million for its Market Investigation References for 2008-09.<sup>2</sup>

**2** The UK's competition regime is largely the result of the Competition Act 1998 and the Enterprise Act 2002, which introduced a range of reforms aimed at protecting consumers and ensuring markets work well. The Government's expectations for the regime are set out in its 2001 White Paper *A World Class Competition Regime*. This stated that:

- competition decisions should be taken by strong, proactive and independent competition authorities;
- the regime should root out all forms of anti-competitive behaviour;
- there should be a strong deterrent effect; and
- harmed parties should be able to get real redress.

There is other legislation which impacts on the UK regime, such as the Communications Act 2003 and the underpinning EU framework. This report covers only those issues arising from the Competition Act 1998 and the Enterprise Act 2002.

**3** To meet these expectations the competition authorities were given a range of new competition powers, and the White Paper made clear the expected relationships between the authorities. For example, the Office of Fair Trading would keep markets under review, and where it considered they were not working well, refer them to the Competition Commission for a full investigation. The impact assessment for the White Paper did not comment on the expected use of the new legislative powers, but there were departmental planning assumptions covering both this and interactions between the authorities. In addition, the Regulators are committed to withdrawing from economic regulation of their markets where practicable, and replacing detailed sectoral rules with the operation of competition law.

<sup>1</sup> [www.offt.gov.uk/shared\\_offt/reports/Evaluating-OFTs-work/oft1102.pdf](http://www.offt.gov.uk/shared_offt/reports/Evaluating-OFTs-work/oft1102.pdf).

<sup>2</sup> Under the Enterprise Act, the Office of Fair Trading, certain economic regulators and the Secretary of State may refer a market to the Competition Commission for review if they suspect that any feature or features of the market prevents, restricts or distorts competition. This is known as a Market Investigation Reference.

**4** The responsibility for implementing the aims of the competition regime rests with a number of public authorities, principally the Office of Fair Trading, and the Competition Commission. The appellate body is the Competition Appeal Tribunal. As the competition regime complements, and often acts as an alternative to, wider economic regulation, it also includes the sector regulators, such as the Office of the Gas and Electricity Markets. For the purposes of this report we have defined the regime as the two main competition bodies (the Office of Fair Trading and the Competition Commission), the Competition Appeal Tribunal, and the sector regulators (henceforth referred to as the Regulators). We have calculated that the resources these organisations devote to their work on competition is about £27 million annually.

**5** It is now nine years since the Government's 2001 Competition White Paper and seven since the enactment of the Enterprise Act. The extent to which the regime is meeting its aims efficiently has come into question from the House of Lords Select Committee on Regulators, and also in the joint Department of Trade and Industry and HM Treasury concurrency review. There is no one body within government that has specific oversight of the competition regime as a whole although the Department for Business, Innovation and Skills has overall responsibility for competition policy. The National Audit Office, however, has audit responsibility for all of its constituent bodies (with the exception of the Civil Aviation Authority). Through our audit work, we have built up a body of evidence on the efficiency and effectiveness with which the system is operating, and the challenges it still faces in meeting its original expectations.

**6** This report brings together that evidence. Its purpose is to inform the debate on the future development of the competition regime, and it will therefore be of particular interest to policy makers and those who operate the regime. It is a systemic review, not a commentary on the performance of the separate organisations within the system. For the competition regime to operate well, it is necessary for each of its constituent organisations to function efficiently and effectively. But that alone is not sufficient to ensure that the performance of the system as a whole is optimal. Factors such as the level of coordination between organisations, the degree of tension between system-level and organisation-level objectives, and the way incentives for taking different courses of action are balanced across different parties affect the extent to which the system is able to meet its expectations. The evidence we have assembled in this report sheds light on some of the key areas that, in our view, should form part of any consideration of the scope for improving the overall operation of the regime.

**7** Our report covers the four main areas of reform introduced by the Competition and Enterprise Acts, and the resourcing of the system as a whole:

- Enforcement of the Competition Act (Part 2)
- Appeals (Part 3)
- Market Investigation References (Part 4)
- Mergers (Part 5)
- Resourcing of the system (Part 6)

## Findings

**8** The system of competition and judicial oversight in the UK is generally effective in meeting its aims, and is well regarded by comparison with international equivalents. For example, ratings in the Global Competition Review (an international journal that annually ranks competition authorities around the world) show that the UK's Office of Fair Trading and Competition Commission are globally recognised as amongst the leading authorities.

**9** However, while the performance of the separate bodies in the system is well regarded, our evidence suggests that the competition regime as a whole still faces a number of challenges to function as intended. Although the system is still relatively young compared to its peers in the US and the European Union and is still developing, it faces challenges in: building a richer body of case law; ensuring that decisions on use of competition powers are not being adversely affected by the length, and uncertainty of outcome; ensuring markets are referred where appropriate to the Competition Commission for independent examination; and allowing a greater flow of expertise and resources around a system that involves a number of different bodies that exercise similar powers but with no over-arching governance arrangements.

**10** In particular, we found that:

- The competition system relies on a richness of case law and precedent setting. Regulators can usually choose to use either their regulatory powers or their competition powers to achieve the desired outcome<sup>3</sup>. However, to date Regulators have used their competition enforcement powers sparingly, with the risk that case law is not as rich as it needs to be. **The Government should evaluate whether the incentives within the system for Regulators to use their competition powers are appropriate to establish the body of case law required for an effective competition system.**
- It is vital that there is an effective system for appealing against decisions taken by the competition authorities and Regulators. The decision process itself is often lengthy; and following a decision, most Competition Act investigations are subsequently appealed. There is a risk that the length, and uncertainty of outcome, of the enforcement process in its entirety may reduce the appetite of the authorities for using their competition enforcement powers. These factors may also encourage greater use of either early resolution to expedite cases, or of regulatory rather than competition powers by the Regulators, than is desirable for the development of the application of competition law in the UK. **The Government should review whether progress in the development of the body of case law has been adversely impacted by these factors.**

<sup>3</sup> There are some exceptions to this such as directions under European law and those given in the Communications Act 2003 requiring the Office of Communications to carry out its own regular market reviews.



- Regulators are not making Market Investigation References to the Competition Commission to the extent envisaged in planning assumptions. The disincentives in the system against referral are: the Regulators' perceived loss of control over the outcome, with any remedies being imposed by the Competition Commission; the length of the process; and the uncertainty created in the industry. **The Government should adopt a presumption that all Regulators actively consider using their powers to make Market Investigation References on a regular basis. The National Audit Office will periodically examine the evidence that they are doing so, and report to Parliament on the extent to which regulators are making use of this important mechanism.**
- The competition regime is overseen by several different government bodies and work flows unevenly round the system, but resources are not managed or funded at a system-wide level to avoid mis-matches between caseload and staffing. This risks suboptimal efficiency and effectiveness at a system level. For example, the Competition Commission's overall caseload reduced from a peak of 17 cases in mid-2007 to five cases in early 2009. **The Government should consider how resources and expertise in the competition regime can be used more flexibly and efficiently. This could, for example, entail the creation of a networked government service of competition experts, to build up public sector-wide expertise and enable more flexible allocation of resources.**

**11** At the end of each part of this report, we set out our more detailed conclusions on what we consider should be key concerns in considering the future development of the competition regime in relation to enforcing competition law, appeals, market studies and investigations, merger control, and the regime's use of resources.

# Part One

## Regime resources oversight and governance

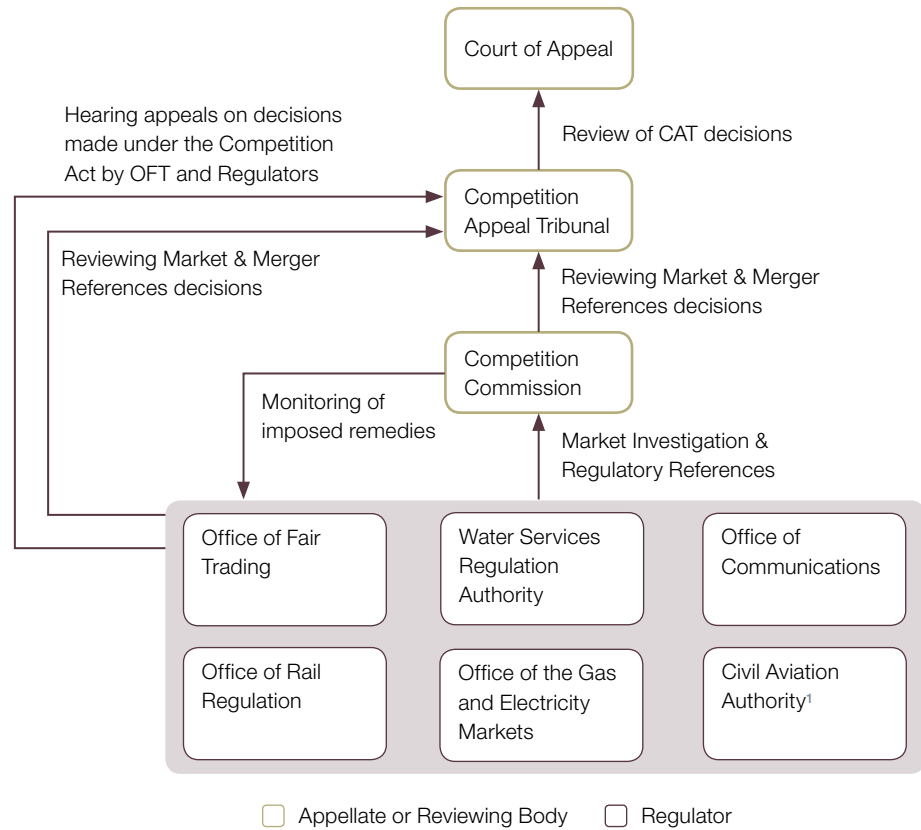
**1.1** The UK's competition regime consists of the Office of Fair Trading, the Competition Commission, the Competition Appeal Tribunal, and a number of Regulators (the Office of Communications, the Office of the Gas and Electricity Markets, the Water Services Regulation Authority and the Office of Rail Regulation). For the purposes of this report we refer to the latter as the Regulators. **Figure 1** shows the relationships between these bodies and their main interactions. This part examines the main activities of the bodies in the system.

**1.2** The Office of Fair Trading is the primary competition authority in the UK<sup>4</sup>; it investigates anti-competitive agreements and conduct, and enforces competition law. The Office of Fair Trading is also the main body empowered to initiate reviews of markets and mergers in the UK. The UK's competition regime was set up with a 'two phase' system for merger control and market investigations. The two phase system allows referrals of markets and mergers by a phase one body to the independent Competition Commission, the phase two body, where a more detailed investigation is warranted. The two phase system does not apply to investigations of anti-competitive agreements or conduct under the Competition Act 1998, where it is the Office of Fair Trading or Regulator which is the decision maker. The Competition Appeal Tribunal is the appellate body in the UK regime.

**1.3** The Regulators were each established by statute, with primary legislation setting out their statutory duties in each of their sectors, for example, ensuring security of supply, or protecting consumers through setting price limits for dominant suppliers. The legislation initially covered the regulation of monopolies or dominant suppliers, with a requirement to promote and introduce competition where appropriate. The Competition Act granted powers to the Regulators (mirroring those of the Office of Fair Trading) to enforce the Act's prohibitions in their respective sectors. In many instances, Regulators can therefore choose to use either their competition powers or their regulatory powers in meeting their statutory duties. There is also European legislation that impacts in particular on the telecommunications sector, containing specific competition duties and powers that are excluded from the scope of this report. Consumer powers can also be an important complement to competition powers, and the Office of Fair Trading uses its discretion in deciding which of its powers to use.

4 In addition to its competition responsibilities, the Office of Fair Trading also has a role in consumer protection.

**Figure 1**  
The UK competition regime



Source: National Audit Office

**NOTES**

- 1 The Civil Aviation Authority has powers to make a market reference of the Air Traffic Control Services market only.
- 2 The Secretary of State may also make a reference to the Competition Commission on grounds of public interest.
- 3 The diagram omits the Supreme Court of the UK and the European Court of Justice, both of which are in the judicial structure which includes the Tribunal. It also omits the Northern Ireland Authority for Utility Regulation.
- 4 The Court of Appeal's jurisdiction only extends to England and Wales. The equivalent court in Scotland is the Court of Session, and in Northern Ireland, the Court of Appeal of Northern Ireland.

## The main activities of bodies in the competition regime

### Competition Act investigations

**1.4** The Office of Fair Trading and the Regulators have powers to investigate whether infringements of the Competition Act 1998 have occurred. The Office of Fair Trading can investigate any business sector for infringements, (including sectors covered by the Regulators), while the Regulators cover their own particular sector. There are arrangements in place for the Office of Fair Trading and the Regulators to agree which is best placed to investigate an alleged infringement in a sector covered by a Regulator to avoid duplication of work.

**1.5** There are two principal types of infringements of competition law, referred to as Article 101 (or Chapter 1) and Article 102 (or Chapter 2) infringements<sup>5</sup>. An Article 101/Chapter 1 infringement involves anti-competitive agreements and covers illegal arrangements to fix prices between competitors, often referred to as a “cartel”, and other forms of agreements which may prevent, restrict or distort competition. An Article 102/Chapter 2 infringement covers the abuse of a dominant position by a company in a particular market. A recent example of an investigation into anti-competitive agreements is the Office of Fair Trading’s case brought against over 100 firms in the construction sector for cover pricing in tender processes (the Office of Fair Trading’s decision is subject to appeal at the Competition Appeal Tribunal). A recent example of an ‘abuse of dominance’ type investigation is the Office of the Gas and Electricity Markets’ decision on National Grid, which found the existence of commercial contracts that had the effect of creating barriers to entering the market.<sup>6</sup> Competition Act investigations are covered in Part 2 of this report.

### Appeals

**1.6** The Competition Appeal Tribunal is the appellate body to whom appeals are made. An appeal may be made to the Competition Appeal Tribunal on any infringement or non-infringement decision made by the Office of Fair Trading or Regulators, on Market Investigation References by the Competition Commission, and on any merger decision made by the phase 1 or 2 bodies. Various aspects of decisions of the Competition Appeal Tribunal can be further appealed to the Court of Appeal. Appeals are covered in Part 3 of this report.

5 These refer to the appropriate Articles of the European Community Treaty and the equivalent legislation in the Competition Act 1998.

6 The Court of Appeal handed down its judgement on this case in February 2010, upholding the finding of breach but further reducing the penalty (the original penalty was first reduced on appeal to the Competition Appeal Tribunal).

## Market studies and investigations

**1.7** The Office of Fair Trading and the Regulators (the phase 1 bodies) are responsible for conducting initial studies of markets<sup>7</sup>. They seek to address any identified problems themselves<sup>8</sup> or via recommendations to government, or they determine whether referral is needed to the Competition Commission (the phase 2 body) for a more detailed investigation. A recent example of a market investigation is the Competition Commission's examination of the airports sector carried out between 2007 and 2009. Market studies and investigations are covered in Part 4 of this report.

## Mergers

**1.8** The UK operates a two phase merger control system: the Office of Fair Trading undertakes an initial scrutiny of any potential mergers that are notified to it, and where appropriate will refer them for a more detailed assessment by the Competition Commission. A recent example of a merger referred by the Office of Fair Trading to the Competition Commission was that proposed between Friends Reunited and Brightsolid (the owner of leading on-line genealogy services in the UK). Mergers are covered in Part 5 of this report.

<sup>7</sup> These may also address consumer issues, or areas where competition and consumer issues overlap.

<sup>8</sup> This can include using their competition enforcement powers.

# Part Two

## Enforcing the Competition Act

**2.1** The Competition Act 1998 came into force in March 2000. It prohibits agreements, decisions and concerted practices which have the object or effect of preventing, restricting or distorting competition within the United Kingdom. It also prohibits the abuse of a dominant position within the United Kingdom<sup>9</sup>. The Act and the new powers granted to the competition authorities and the expectations of the system were outlined in the Government's 2001 White Paper *A World Class Competition Regime*.

**2.2** The exercise of competition powers is important in giving the law force by establishing a rich body of case law and legal precedents. It also provides clarity to businesses on the 'rules' within which they must operate in their market interactions.<sup>10</sup> Infringement decisions, where the party is found to have infringed the law, also act as a deterrent against anti-competitive behaviour.

**2.3** The White Paper was silent on expectations for the volume of cases, the proportion of infringements to non-infringement decisions, and the use of competition powers by Regulators as opposed to their regulatory powers, but did state that the use of powers should create a strong deterrent effect.

**2.4** This Part sets out:

- the use of competition powers by the various parties in the system, including the balance of incentives on Regulators of whether to use competition or regulatory powers and the levels of redress to date; and,
- measurement of the deterrent effect.

9 The UK regime fits within the EC regime: the Modernisation Regulation (01/03) requires Member States' competition bodies to apply EC law where there is an effect on trade between Member states. Action by the EC Commission (in mergers, cartels, abuse of dominance and vertical agreements) must be taken into account.

10 In this regard, EC decisions can also provide precedents for the purpose of enforcing competition law in the UK.

## Use of competition powers

### Volume of cases

**2.5** In total the Office of Fair Trading has made 43 competition enforcement decisions (**Figure 2**) since 2000. In the majority of cases where the Office of Fair Trading found a breach, a fine was imposed on the firm, for example, in September 2009 the Office of Fair Trading fined over 100 construction firms nearly £130 million for cover pricing in tender processes (a number of firms have appealed the decisions and or fines against them to the Competition Appeal Tribunal). The total amount of the fines imposed in the UK under the Competition Act (and Articles 101 and 102) by 1 January 2010 was £322 million.<sup>11</sup> On appeal to the Competition Appeal Tribunal some of the fines were reduced, making the net total amount of fines imposed in the order of £298 million.<sup>12</sup>

**2.6** In a further three cases in the last three years (airline fuel surcharges, dairy products, and tobacco) parties have provisionally agreed to pay fines totalling up to £373 million. In 2008 the Office of Fair Trading secured criminal convictions and director disqualification orders against company executives in one case, and is pursuing charges in another. The Office of Fair Trading estimates the direct financial benefit to consumers from its competition enforcement work at £78 million per year on average for the period 2006-09.<sup>13</sup>

### Figure 2

The number of competition enforcement decisions by the Office of Fair Trading and Regulators since 2000

Office of Fair Trading	Office of Communications	Office of the Gas and Electricity Markets	Office of Rail Regulation	Water Services Regulation Authority	Total
43	23	4	7	2	79

Source: National Audit Office analysis of Office of Fair Trading's public decision register

#### NOTE

The Competition Act 1998 came into force in March 2000.

11 This figure takes into account reductions in penalties in the light of successful leniency applications: the figure excludes the potentially significant fines that undertakings have agreed to pay in the Airline fuel surcharges, Dairy Products and Tobacco cases since the Office of Fair Trading has yet to adopt 'decisions' to that effect.

12 In addition, some of the fines have been reduced subsequently on appeal to the Court of Appeal.

13 The Office of Fair Trading does not include in this estimate the benefits arising from deterrence, precedent setting, or informal advice.

**2.7** Unlike the Office of Fair Trading, Regulators have the option to use their regulatory powers, for example, by enforcing and (where appropriate) modifying licence conditions, rather than using competition powers. The exception to this is in the communications sector, where companies can raise a dispute with the Office of Communications in such a way that the Regulator has to use its regulatory powers rather than its competition powers.<sup>14</sup>

**2.8** Our analysis shows that Regulators have, to date, favoured using their regulatory powers rather than their competition powers. The Regulators have in total made 36 infringement or non-infringement competition decisions since the Competition Act came into force in March 2000. Of these, the Office of Communications (and its predecessor the Office of Telecommunications) has made 23 decisions, representing over 60 per cent of the total, with the other three Regulators making between two and seven decisions each (Figure 2).

**2.9** We analysed the balance of incentives on the Regulators between using their competition powers, or their regulatory powers (**Figure 3**). We found from our interviews with Regulators that there were three main disincentives against the use of competition powers. These were: the potential duration of Competition Act cases; the difficulty of proving an infringement and the resource commitment; and, the impact on their own limited resources when compared to using regulatory powers.

### Infringement versus non-infringement

**2.10** An infringement decision has a strong deterrent effect, establishes case law, and can result in a financial penalty, adverse publicity and scope for private damages actions against the guilty party or parties. It also has the potential to replace a body of regulations in a regulated sector. Non-infringement decisions are helpful in terms of clarifying the law, and in setting a precedent, but they are unlikely to have as strong a deterrent effect on anti-competitive behaviour as an infringement decision. They can, however, create a deterrent effect if a third party assumes the burden of proof and seeks to prove the existence of an infringement.

<sup>14</sup> Where companies raise a dispute, the Office of Communications' decision can be appealed.



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**Figure 3**

## Perceived incentives for and against use of competition enforcement powers by Regulators

**Incentives in favour of their use**

- Enforcement action increases deterrence both in terms of the immediate danger to a business of incurring a fine, and the wider signal that the competition regulators are active.
- It reduces consumer detriment by stopping anti-competitive behaviour.
- It can bring greater clarity for businesses through explaining how the law applies, and establish market 'rules' in the industry. Case law on appeals can also provide a very useful source of guidance.
- It can establish clear precedents which focus on the economic 'effects' which makes it difficult for companies to exploit any uncertainties as to how the law would be enforced and may, therefore, provide scope for the Regulator to reduce significantly the resources it devotes to regulatory interventions in the market.
- A steady flow of cases will render the workings of markets more transparent and this will aid the understanding of participants in those markets, new entrants and consumers.
- It would potentially open up potential for follow-on private actions for damages to compensate customers, to act as an extra deterrent.
- A vibrant caseload dealing with interesting high profile issues will attract high calibre staff to the competition regulators and motivate existing staff.

**Incentives against their use**

- The potential length of an investigation against generally well-resourced parties with strong commercial interests to protect, and the expected resource commitment over several years (including appeals) can be significant; (the so-called "war of attrition").
- The difficulty in concluding a case expeditiously will potentially reduce the availability of resources for other priority work. In addition, there is the potential expense of bringing additional resources to bear.
- The likely complexity of the investigation, and the difficulty of proving an infringement (in particular in abuse of dominance cases). In addition, Regulators' lack of experience of cases involving price-fixing or illegal agreements.
- Potentially bodies may prefer an alternative course of action for a number of reasons (for example, it is believed to be more cost effective and/or efficient; a lack of staff experience in dealing with competition enforcement investigations).
- Competition law can take a very long time to provide a resolution for consumers. Where the detriment is spread across a wide group of consumers and there is no prospect of follow-on action, regulation can be more effective in providing compensation/redress for end consumers.
- There will be uncertainty about the outcome that could leave important regulatory issues unresolved until the case is concluded.

Source: National Audit Office

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**2.11 Figure 4** shows the split between infringement decisions and non-infringements. In the ten years or so since the Act came into force, the Office of Fair Trading has made a slightly greater number of infringement decisions (24) than non-infringement decisions (19). In the same period, however, the Regulators have in total reached only two infringement decisions. A lack of infringement decisions risks, over time, lessening the deterrence effect of competition powers.

### Cartels and abuse of dominance

**2.12** The aims of the 2001 Competition White Paper were to address both the abuse of a dominant position, and the existence of anti-competitive agreements, including cartels. **Figure 5** shows that the Office of Fair Trading's infringement decisions cover both the abuse of a dominant position (Article 102/Chapter 2) and cartels or agreements (Article 101/Chapter 1). By contrast, the Regulators' infringement decisions have all related to the abuse of dominance (Article 102/Chapter 2). Complaints about abuse of dominance are much more common in the regulated sectors due to the regulated industries having traditionally been dominated by incumbent businesses that, once privatised, retained near monopoly or significant market power.

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#### **Figure 4**

Infringement and non-infringement decisions by the Office of Fair Trading and Regulators since 2000

	<b>Infringements</b>	<b>Non-infringements</b>
Office of Fair Trading	24	19
<b>Total (for Office of Fair Trading)</b>	<b>24</b>	<b>19</b>
Office of Communications <sup>1</sup>	0	23
Office of the Gas and Electricity Markets	1	3
Water Services Regulation Authority	0	2
Office of Rail Regulation	1	6
<b>Total (for Regulators)</b>	<b>2</b>	<b>34</b>
<b>Total Overall</b>	<b>26</b>	<b>53</b>

*Source: National Audit Office analysis of Office of Fair Trading's public decision register*

#### **NOTE**

1 Includes the predecessor body, the Office of Telecommunications.

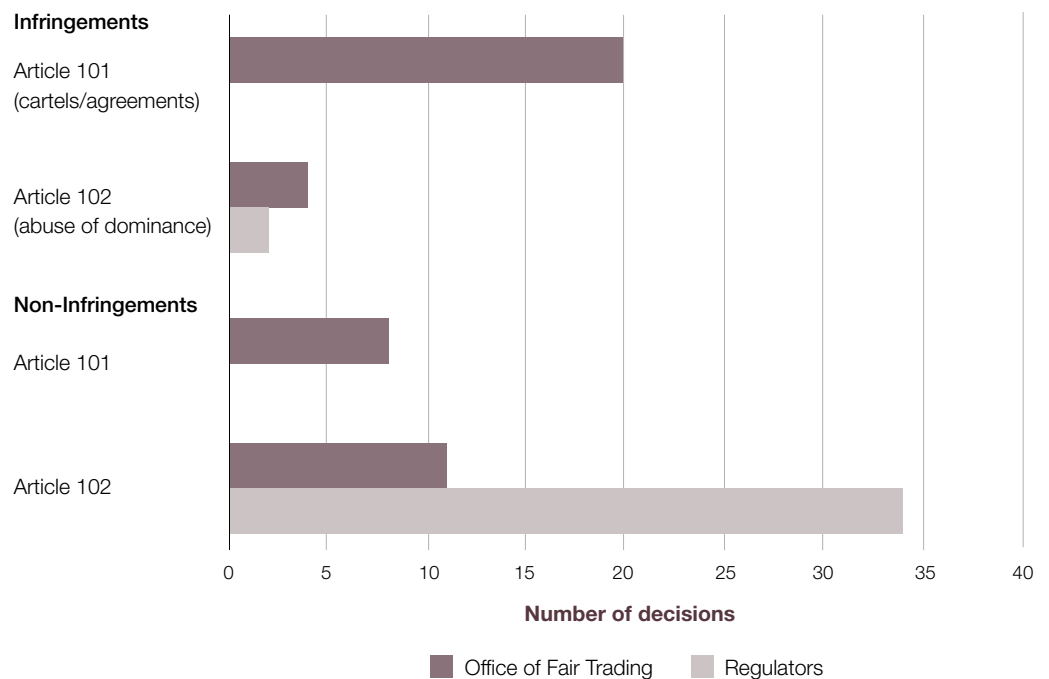
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## Abuse of dominance

**2.13** Figure 5 shows non-infringement decisions are more likely to be reached on abuse of dominance cases (Article 102/Chapter 2) than for anti-competitive agreements or cartels (Article 101/Chapter 1). Regulators informed us that this was due in part to the relative difficulty of providing strong, compelling and conclusive evidence to prove an abuse of dominance, unlike a cartel case (Article 101/Chapter 1) where a leniency application (when a member of a cartel applies for immunity from civil penalties and prosecution by providing evidence of the cartel to the Office of Fair Trading or a Regulator) can provide compelling evidence of a cartel.

**Figure 5**

Analysis of type of decisions made by the Office of Fair Trading and the Regulators



Source: National Audit Office analysis of Office of Fair Trading's public decision register

**NOTE**

The Regulators' decisions have all been under Article 102/Chapter 2.

## Cartels

**2.14** The Office of Fair Trading has a policy of raising awareness of the process of leniency, in order to encourage market participants to come forward with evidence of cartel activity. The leniency policy has led to a number of major investigations and infringement decisions against alleged cartels. Recent examples include the Construction Recruitment Forum and the construction industry investigations. In 2008-09 the policy generated some 31 applications for leniency (involving 22 separate cases). The Office of Fair Trading publicises its leniency policy including using publicity from its infringement decisions that started from leniency applications.

**2.15** In each of the sectors covered by the Regulators there is competition in the sub-markets for goods and services, and large parts of the energy and telecoms markets are competitive, where the possibility of cartels exists. The Regulators do not, however, formally publicise the existence of the Office of Fair Trading's leniency policy to the companies in their own regulated sectors, with the consequent risk that companies might not be aware of it.

## Measuring the deterrent effect

**2.16** Measuring the deterrent effect of competition enforcement is important in evaluating the impact of action taken by the competition authorities.

**2.17** The Office of Fair Trading is one of only a few competition authorities globally to have attempted to measure the deterrent effect from its enforcement of competition law. Its research indicates that the ratio of potentially anti-competitive behaviour (agreements and initiatives abandoned or significantly modified) deterred for each of its decisions was: at least 4:1 for abuse of dominance, at least 5:1 for cartels and 7:1 for commercial agreements. The survey results also ranked the most significant deterrence factors as criminal enforcement (and other personal sanctions), fines and adverse publicity. In addition there is a European Union dimension, as enforcement action against anti-competitive practices by the European Commission can also have a deterrent effect on businesses in the UK.

**2.18** The Regulators do not attempt to measure the deterrent effect of their activities.

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### **Key concerns for debate**

- The development of case law is an essential component of establishing an effective competition regime, but to date, most Regulators have made limited use of their competition enforcement powers. The system disincentives, such as the perceived potential length of a competition investigation (including the likelihood of an appeal), its resource-intensive and complex nature, and the uncertainty of outcome, appear to be working against establishing a richer body of case law.
  - Infringement decisions and the consequent fines and bad publicity are an important component of creating a deterrence effect, but, to date there have been only two infringement decisions in the regulated sectors. If more infringement decisions were reached it would increase, over time, the deterrent effect of competition law, and scope for follow-on private damages actions that can bring redress for consumers. Furthermore, it would establish strong legal precedents which may create scope to reduce the need for detailed regulation in some sectors.
  - The Office of Fair Trading has developed an expertise in cartel investigations and is the only body empowered to bring the criminal cartel sanction. Regulators have limited experience of this type of investigation, and could do more to publicise the leniency policy to encourage immunity applications from companies in their sectors that could be involved in cartels. The Government could consider giving the Office of Fair Trading the lead on cartel enforcement across the competition regime as a whole, supported by sector specialists seconded as and when cases arise in regulated sectors.
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# Part Three

## Appeals

**3.1** The 2001 Competition White Paper stated that decisions should be taken by independent competition authorities. An appeals process is an essential part of ensuring the independence of the regime, and is also required to comply with the European Convention on Human Rights in the UK. This appeals function is fulfilled by the Competition Appeal Tribunal.

**3.2** This part examines the volume of appeals, their length, and considerations in the use of appeals. Appeals can be made against Competition Act cartels and abuse of dominance decisions, as well as against market investigation and merger decisions.

### The Competition Appeal Tribunal

**3.3** The Office of Fair Trading's and Regulators' Competition Act powers are considerable because they combine the roles of investigator, prosecutor and adjudicator. To balance this, and to ensure compliance with the European Convention of Human Rights which requires that there should be an appeal of decisions to a court of "full jurisdiction", the Competition Act provides for a right of full appeal ("on the merits") to the Competition Appeal Tribunal<sup>15, 16</sup>. There are also rights to subsequent levels of appeal, to the Court of Appeal and ultimately to the Supreme Court.

**3.4** Appellants are typically main parties alleged to have infringed competition law, in the decisions of the Office of Fair Trading or the Regulator, or they are third parties. Beyond the Competition Appeal Tribunal, parties to a case may appeal on a point of law or as to the amount of the penalty, to the Court of Appeal. Appeals to the Competition Appeal Tribunal, however, on decisions to refer issues to the Competition Commission under the Enterprise Act, and on the Commission's decisions themselves, are considered on the basis of a judicial review of the decision making process, rather than on the merits of the case.

15 Section 12 of the Enterprise Act 2002 created the Competition Appeal Tribunal. Previously the appeals tribunals of the Competition Commission heard appeals under the Competition Act. This arrangement was no longer considered appropriate because the Tribunal can hear applications for review of decisions made by the Commission under Parts 3 and 4 of the Enterprise Act 2002.

16 Other decisions of the Office of Fair Trading and the Regulators under the Competition Act may be challenged by way of judicial review before the Administrative Court.

## Volume of appeals

**3.5** With the competition bodies exercising significant powers to impose fines (or to divest assets in mergers), we found that there are strong incentives in the system to appeal against a decision. Appellants have a reasonable prospect of the fine, parts of the decision, or even the decision itself, being overturned, although if unsuccessful the Competition Appeal Tribunal normally awards the costs against the appellant. Where significant sums of money are concerned, the financial incentive to appeal is strong, as the potential benefits (overturned or reduced fines, as well as avoiding or reducing the potential scope for follow on actions for damages) are likely to outweigh significantly the parties' legal costs. In addition, extending the legal process until all levels of appeal have been exhausted can increase the pressure on a Regulator's resources by extending the timescales and adding to their costs; defer payment of any fine that is payable; and enable the appellant to carry on benefiting from potentially anti-competitive practices.

**3.6** The incentives to appeal have contributed to most decisions made by the Office of Fair Trading or the Regulators under the Competition Act resulting in an appeal to the Competition Appeal Tribunal, with 42 appeals in total since the Act came into force.<sup>17</sup> Roughly three-quarters of them were appeals against the Office of Fair Trading, and the remainder were against Regulators.<sup>18</sup>

**3.7** The following factors contribute to there being a high likelihood of a decision being appealed:

- the relative immaturity of the new regime;
- the great importance of decisions for the immediate parties, the relevant industry and the wider public interest;
- the fact that those contesting the decision are likely to be powerful and well resourced undertakings; and
- the highly complex subject matter;

## Length of the competition enforcement process

**3.8** Competition enforcement investigations can typically take a number of years before a decision is reached, and at the end of this process, there is currently a high likelihood of the decision being appealed. A perception persists amongst Regulators and the Office of Fair Trading that the UK enforcement system, including the likelihood of an appeal, is an onerous process compared with the use of other powers.

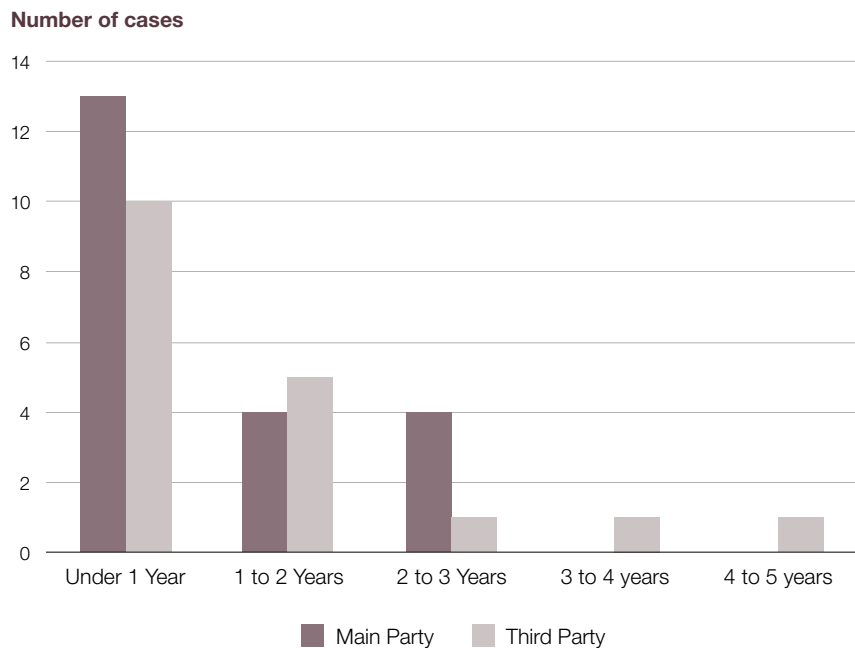
<sup>17</sup> A very small number of the judgments by the Competition Appeal Tribunal have been appealed to the Court of Appeal.

<sup>18</sup> These are mainly appeals against infringement or non-infringement decisions, but also include 10 appeals concerning the jurisdictional issue of whether in fact and law the Office of Fair Trading/Regulator has made an appealable decision. In five of those cases it was found that action taken by the Office of Fair Trading/Regulator did constitute an "appealable decision" under the Competition Act, and in the other five the action taken did not give rise to such a decision, and therefore the Competition Appeal Tribunal had no jurisdiction.

**3.9** Figure 6 shows the timescales of appeals to the Competition Appeal Tribunal against enforcement decisions. The length of the appeal process from the lodging of the appeal with the Competition Appeal Tribunal to the Competition Appeal Tribunal's final judgment (including where it has remitted cases back to the Regulator or competition authority for further work and subsequent hearings by the Competition Appeal Tribunal), varies in length. In the majority of appeals (some 60 per cent) the process has taken a year or less to complete. A further 35 per cent took between one and three years.

**3.10** The remaining two cases took more than three years to conclude, both were appeals against Regulator decisions. These cases are exceptional because they involved matters being remitted back by the Competition Appeal Tribunal to the Regulator for further work or re-investigation during the lifetime of the appeals proceedings. These cases can perhaps be seen as atypical of the appeals process, and have raised complex matters of importance to the industries concerned which have taken a number of years to determine.

**Figure 6**  
Competition Act – length of cases appealed



Source: National Audit Office analysis of the Competition Appeal Tribunal's website

**NOTES**

- 1 Main parties are the target of an infringement decision, whilst third parties are typically the party that made the original complaint.
- 2 The timescales on the cases in excess of three years have involved the remitting back of the decision to the decision-making body for further work or re-investigation.
- 3 Excludes on-going appeals at the Competition Appeal Tribunal and excludes appeals beyond the Competition Appeal Tribunal to the Court of Appeal.



**3.11** Whilst an appeals process can be onerous, there are advantages in an appeal where a competition body wishes to establish a strong legal precedent. A judgment that upholds or rejects a point of law established during the appeal process creates a more robust precedent than one not tested at appeal.

**3.12** Where it considers it appropriate, the Office of Fair Trading uses early resolution to try to expedite some of its investigations. This is where it considers that it may save resources for the Office of Fair Trading (and also for the parties involved), whilst not undermining the deterrent effect, or the Office of Fair Trading's leniency policy.<sup>19</sup> The Office of Rail Regulation also used early resolution on its one infringement decision. Early resolution is likely to reduce the number of appeals to the Competition Appeal Tribunal because it is inherent in an early resolution agreement that parties agree to make admissions and pay a (reduced) financial penalty. The loss of opportunity for a novel or precedential legal point to be tested on appeal needs to be weighed up by the Office of Fair Trading and the Regulators when deciding whether to use Competition Act powers with early resolution or their regulatory powers.

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### **Key concerns for debate**

- It is vital that there is an effective system for appealing against decisions taken by the competition authorities and Regulators. The decision process itself is often lengthy; and following a decision, most Competition Act investigations are subsequently appealed. There is a risk that the length, and uncertainty of outcome, of the enforcement process in its entirety may reduce the appetite of the authorities for using their competition enforcement powers. These factors may also encourage greater use of either early resolution to expedite cases, or of regulatory rather than competition powers by the Regulators, than is desirable for the development of the application of competition law in the UK. **The Government should review whether progress in the development of the body of case law has been adversely impacted by these factors.**

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<sup>19</sup> The National Audit Office Report *The Office of Fair Trading: Progress Report on Maintaining Competition in Markets* HC 127 Session 2008-2009 found that the Office of Fair Trading had reached early resolution agreements in three of its 14 ongoing cases.

# Part Four

## Market studies and investigations

**4.1** The Enterprise Act 2002 gave powers to the Office of Fair Trading and the Regulators to carry out market studies. If these bodies suspect that any feature or features of the market prevents, restricts, or distorts competition they may refer the market to the Competition Commission for review. This is known as a Market Investigation Reference.

**4.2** The Act stipulated that the Competition Commission should carry out its own full investigation of the market from a competition perspective, and develop remedies where appropriate. It set a statutory deadline of 24 months for the length of the investigation, but made no mention of the level of activity that was expected.

**4.3** The intention of referring a market to the Competition Commission is that the market is examined objectively by an expert body with the power to impose remedies that can open up or strengthen competition in the market. The anticipated benefits from Market Investigation References are estimated to significantly outweigh the costs. The Competition Commission has calculated an aggregate consumer benefit of £295 million for 2008-09 for Market Investigation References arising from cases handled by the Competition Commission and the Office of Fair Trading.

**4.4** This Part of our report examines the volume, costs and timescales of cases, and the use of the power to refer markets to the Competition Commission.

### Caseload

**4.5** Planning assumptions at the Competition Commission and at the then Department of Trade and Industry envisaged about four Market Investigation References per year to the Commission: three from the Office of Fair Trading and one from a Regulator. The actual number of references has been much lower. In total, there have been ten referrals to the Competition Commission since 2002<sup>20</sup>, nine of which have been by the Office of Fair Trading (**Figure 7**). To date only one market has been referred by a Regulator to the Competition Commission (the Office of Rail Regulation's decision to refer the rail rolling stock market) and in one other case a Regulator has accepted undertakings in lieu of a reference to the Competition Commission (the Office of Communications' decision not to refer the local loop part of the telecoms market).

20 The most recent market referral was the Office of Fair Trading's referral of local bus markets in January 2010.

## Referrals by the Office of Fair Trading

**4.6** In 2008, in response to the evidence that the Market Investigation Reference system was not operating as intended, the Competition Commission and the Office of Fair Trading conducted an internal joint evaluation. The evaluation was also in response to particular concerns of the Chairman of the Competition Commission that full use was not being made of the Competition Commission's expertise and experience, and that competition enforcement in the UK may therefore not be as effective as it could be.

**4.7** The review identified concerns about the way the regime was operating, and about relations between the Competition Commission and the Office of Fair Trading, in particular:

- inefficient use of resources between the two bodies;
- some concern that the Office of Fair Trading preferred to do its own market studies and ought to be referring more of them to the Competition Commission; and
- that while the Market Investigation Reference process could lead to the imposition of significant remedies, it was comparatively high cost, inflexible and occasionally appeared ineffective.

**4.8** The review found that there was insufficient communication and coordination between the Competition Commission and the Office of Fair Trading, and it made a number of recommendations for how the system could be improved, including reducing timescales for less complex and smaller Market Investigation References<sup>21</sup>, greater sharing of information and more secondments.

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### Figure 7

Markets referred to the Competition Commission under the Enterprise Act

	Markets referred
Office of Fair Trading	Store card credit services, Classified directory advertising services, Home credit, Domestic bulk liquefied petroleum gas, Northern Ireland personal banking, Groceries, Payment protection insurance, BAA Airports, Local bus services
Office of Communications <sup>1</sup>	None
Office of the Gas and Electricity Markets	None <sup>2</sup>
Water Services Regulation Authority	None
Office of Rail Regulation	Rolling stock leasing market

Source: National Audit Office analysis of Competition Commission's website

#### NOTES

- 1 Includes the predecessor body the Office of Telecommunications.
- 2 The storage and transportation elements of the gas market were referred to the Competition Commission's predecessor – the Monopolies and Mergers Commission – in 1993 and 1996.

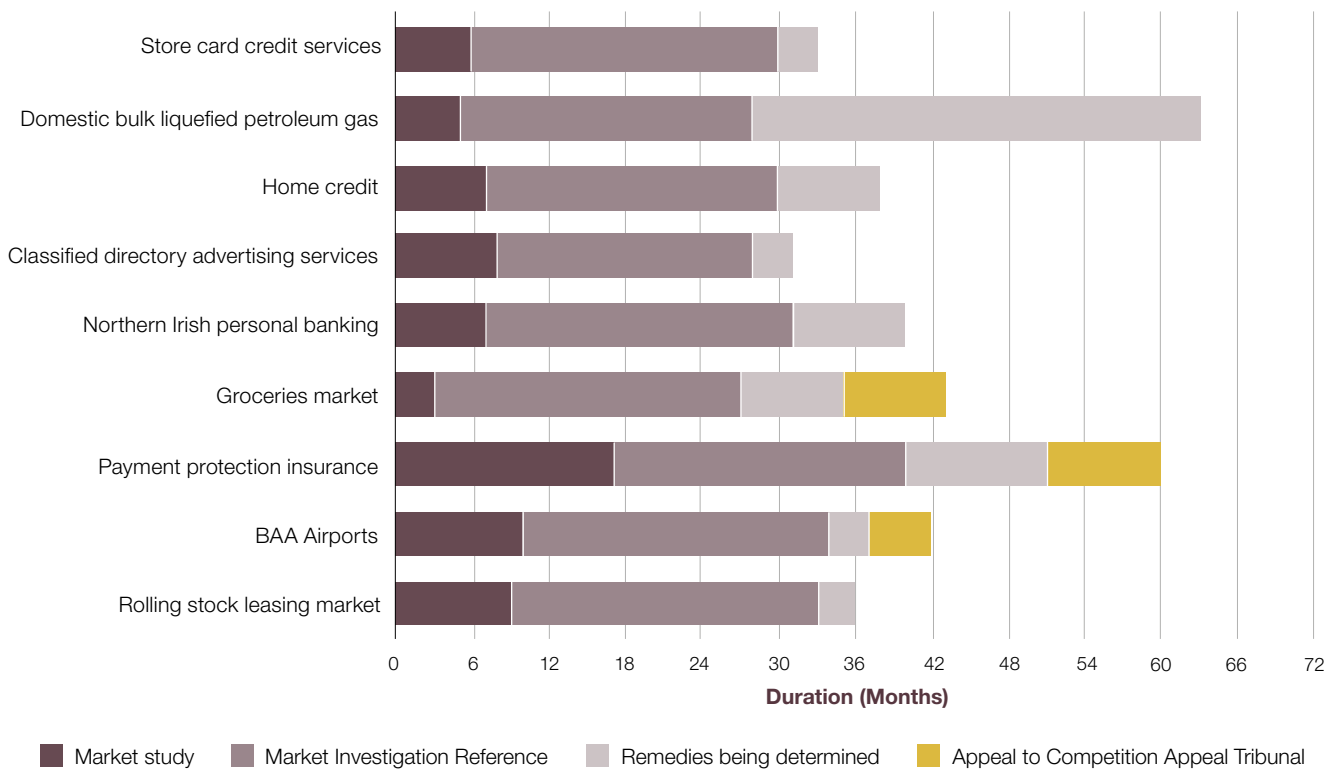
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21 The Competition Commission now aims to conduct its Market Investigation References in no more than 18 months.

**4.9** The review also found that, whilst the Competition Commission had used no more resources at an organisational level than originally planned, all but one of the Market Investigation References had taken longer than the 11-14 months expected in the Competition Commission's original planning assumptions, with only one of the six completed Market Investigation References reporting appreciably before the 24-month statutory deadline. **Figure 8** shows that the whole process from the initiation of the Office of Fair Trading's market study to the final determination of remedies can take considerably longer than 24 months, and it can be lengthened yet further where there is an appeal.

**4.10** Costs of Market Investigation References had also been higher than the expected level of £1.25 million estimated in 2002 planning documents, with a range of actual costs from £1.20 million (Domestic bulk liquefied petroleum gas) to £5.06 million (Groceries).

**Figure 8**  
Timescales of market studies/market investigations



Source: National Audit Office analysis of Competition Commission website data

**NOTE**

The cases are ordered chronologically based on the date of referral, with store card credit services being the earliest which was referred to the Competition Commission in March 2004.

## Referrals by the Regulators

**4.11** The planning assumption at the Competition Commission and at the then Department of Trade and Industry of one referral a year by a Regulator to the Competition Commission has failed to materialise, and to date the Office of Rail Regulation is the only Regulator to have referred a market (the rolling stock leasing market) to the Competition Commission. Instead, the Regulators have relied on their regulatory powers or the threat of a reference to investigate their markets. Furthermore, all the Regulators carry out their own regular market reviews. For example, the Office of Communications, which is required by European law to review product and service markets identified by the European Commission on a rolling basis.

**4.12** We examined the incentives on Regulators to refer a market to the Competition Commission to understand why the number of references has been much lower than anticipated (**Figure 9**). In our discussions with Regulators we found that the main disincentives against referral that they perceived were a loss of control over the outcome and the remedies imposed by the Competition Commission, the length of the process, and the uncertainty created in the industry.

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### Figure 9

Perceived incentives for and against use of market referral powers by Regulators

#### Incentives in favour of their use

- The Competition Commission is a highly-regarded, expert body that can provide an objective look at a market, whereas the Regulator, having itself shaped the regulation of the market, may find it more difficult to step back and critically examine it.
- There are potential benefits for consumers in the industry from increasing competition (lower prices, higher quality).
- Using referral powers can demonstrate to the industry that the Regulator is prepared to refer a market if the industry does not comply with its wishes.
- The Competition Commission has power to make structural remedies that some Regulators do not have under existing legislation.
- By referring the market to the Competition Commission the Regulator can avoid the resource costs of a market review, which it would otherwise incur.

#### Incentives against their use

- The loss of control and the uncertainty of the outcome for the Regulator.
- The potential length of the process, compared to alternative regulatory routes.
- The cost of the process for industry including the costs of potential appeals.
- A concern that a competition body unfamiliar with the industry might give too much weight to competition considerations and not properly balance various “public interest” considerations.
- The uncertainty of the outcome for the industry, and the possible investment hiatus in the industry until the outcome is known. The more lengthy and unwieldy the process, the more of a threat it is to the industry.

Source: National Audit Office

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**4.13** We carried out four case studies of the different regulated sectors to examine how Regulators had used a market reference, or how they had used their regulatory powers to conduct their own market reviews of competition in their sectors in preference to a reference. These show that a variety of approaches have been adopted where the Regulators felt that competition is ineffective. **Figure 10** provides examples of market review activity in the regulated sectors, the length of the process and the outcomes.

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### **Figure 10**

#### Case studies of recent market reviews of regulated markets

##### **Office of Communications: BT undertakings in lieu of a reference to the Competition Commission**

In December 2003 the Office of Communications launched a review of the telecommunications sector which lasted for just over two and half years (as the national telecoms regulator, the Office of Communications is required by EU regulations to undertake a range of market reviews every three years). In its review, the Office of Communications found evidence of market problems in the local loop part of the market that it considered reached the threshold that would allow the Office of Communications to refer the market to the Competition Commission. The Office of Communications decided to refer the market, but BT plc offered undertakings that addressed the Office of Communications's concerns. Over 230 separate undertakings were offered by BT in lieu of a formal reference to the Competition Commission. The undertakings allowed the break-up of some of the company, including the splitting off of Openreach into a separate independent arms-length business, and they increased access for competitors to the BT network including local loop access. The acceptance of these undertakings led to no further investigative action and no referral being made to the Competition Commission.

##### **Office of the Gas and Electricity Markets: Energy Probe using regulatory powers**

The Office of the Gas and Electricity Markets Energy Probe launched in February 2008 focused on the retail market and the consumer and supplier perspectives of the barriers to switching suppliers, competitiveness of pricing, and availability of information. Using its formal information-gathering powers under the Enterprise Act 2002, the Office of the Gas and Electricity Markets required suppliers to provide information, and after a six-month investigation the Office of the Gas and Electricity Markets published its findings that concluded that more work was required to accelerate competition, and that there were concerns surrounding differential pricing, vulnerable consumers, low customer information and barriers to entry/expansion. After a further nine months, developing and consulting on remedies, the Office of the Gas and Electricity Markets used the threat of a Market Investigation Reference to the Competition Commission to influence suppliers to sign up to the proposed amendments to licences. These introduce information obligations that should help assist consumers in switching and measures to reduce price differentials and tougher rules on mis-selling. Overall the process from starting the probe to implementing remedies took 18 months.

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**Figure 10**

Case studies of recent market reviews of regulated markets continued

**Office of Rail Regulation: Market Investigation Reference – Rolling Stock Leasing Market**

The Office of Rail Regulation commenced a review into the rolling stock market in July 2006, and after a nine-month investigation decided to refer the market to the Competition Commission. The Office of Rail Regulation investigation was driven by a submission from the Department for Transport raising concerns about the possible exercise of monopoly power in the market, and by its own concerns of competition problems in the rolling stock leasing market that had the potential to lead to higher prices and a poorer quality of service than would otherwise be the case in a more competitive environment. The Office of Rail Regulation considered this information and then made the referral to the Competition Commission. The Competition Commission completed its investigation within two years. It found that there were features in the market which were having an adverse effect on competition and on rail users. The Competition Commission imposed undertakings after consultation, these were aimed at introducing greater competition mainly through greater choice.

**Office of Fair Trading: Airport Review**

The Office of Fair Trading launched a market study in June 2006 into the UK Airports sector, and decided to refer the case nine months later to the Competition Commission. After a two year investigation, the Competition Commission concluded that the BAA dominance was a feature which adversely affected consumers. The Competition Commission proposed undertakings that set out the sale of various sites including Gatwick and changes to consultation processes for services at Heathrow. These undertakings were appealed to the Competition Appeal Tribunal. BAA won on one of the two points that were raised in its appeal against the Competition Commission.

*Source: National Audit Office analysis of Regulators' and OFT's websites*

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**Key concerns for debate**

- The system was intended to generate a much higher level of market investigation references than has been the case. There is a risk that the incentives for and against referral are not balanced appropriately, resulting in a lack of references to the Competition Commission. Furthermore, the threat of a reference to the Competition Commission becomes less credible the longer a Regulator goes without using this power.
  - The relationship between a Regulator and the industry it regulates is different from that between a competition body such as the Office of Fair Trading and industry. There is a risk that the Regulator looks differently at competition issues within their industry and that this could colour their view of the potential benefits of referring their market to the Competition Commission.
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# Part Five

## Mergers

**5.1** The Enterprise Act 2002 substantially altered the merger control regime in the UK by removing ministers from decision-making and replacing a 'public interest' test with an assessment of whether a merger would result in a 'substantial lessening of competition'. The Act also made the Office of Fair Trading responsible for monitoring the undertakings and orders imposed on merging parties. This part examines the merger control regime in terms of its use of resources, the duration of merger investigations, and the performance of the regime.

### The UK merger regime

**5.2** The UK operates a two phase merger control system. The Office of Fair Trading undertakes an initial scrutiny (Phase 1 review) of each case and decides whether to clear the merger, to impose remedies or to refer it to the Competition Commission (Phase 2 review) if it considers the merger raises potentially significant competition issues which merit an in-depth assessment.

**5.3** There is no obligation on companies that wish to merge to pre-notify the merger to the Office of Fair Trading. In practice, however, most firms voluntarily notify mergers to the Office of Fair Trading as the competition authorities have the power to require a merger to be reversed if it is judged by them to cause a substantial lessening of competition in the market.

**5.4** In contrast to measures in the Competition Act, the Regulators have no powers in terms of merger control, although they are consulted by the Office of Fair Trading where the merger involves companies in their sector.<sup>22</sup> In addition, the mergers regime does place statutory limits on the length of certain parts of the investigative process, to lessen the impact of undue delay on the ongoing business of the referred firms.

### Volume of mergers and appeals

**5.5** The overall volume of mergers investigated at Phase 1 indicates that the proportion has reduced from 28 per cent of all known UK mergers in 2004-05 to 13 per cent in 2008-09 (**Figure 11**). **Figure 12** indicates that the number of mergers referred and the number requiring remedy varies from year to year.

<sup>22</sup> The only exception is in the water industry where all mergers of companies with turnover in excess of £10 million are automatically referred to the Competition Commission, and the test applied is not the substantial lessening of competition but whether the merger may be expected to prejudice the Water Services Regulation Authority's ability to make comparisons.



**Figure 11**

The number of merger cases investigated and referred by the Office of Fair Trading

	<b>Total Mergers</b>	<b>Investigated (percentage of total mergers)</b>	<b>Qualifying</b>	<b>Referred (percentage of qualifying mergers)</b>	<b>Undertakings in lieu of Referral (percentage of qualifying mergers)</b>
2004-05	910	257 (28%)	144	18 (12%)	5 (3%)
2005-06	1,006	242 (24%)	143	17 (12%)	4 (3%)
2006-07	961	131 (14%)	103	13 (13%)	7 (7%)
2007-08	1,061	112 (11%)	97	10 (10%)	5 (5%)
2008-09	656	84 (13%)	72	7 (10%)	6 (8%)

Source: National Audit Office analysis

**Figure 12**

The number of merger references that the Competition Commission has dealt with in each year since 2004

	<b>Number of cases</b>	<b>Requiring remedies (percentage of cases)</b>	<b>Not requiring remedies (percentage of cases)</b>
2004-05	17	5 (29%)	8 (48%)
2005-06	15	3 (20%)	8 (53%)
2006-07	13	7 (54%)	4 (31%)
2007-08	9	1 (11%)	4 (44%)
2008-09	7	4 (57%)	2 (29%)

Source: National Audit Office analysis

**NOTE**

Figures do not sum with total number of cases as cancelled references and ongoing investigations are excluded.

**5.6** The number of merger references received by the Competition Commission has reduced in particular since 2007-08. The Competition Commission and the Office of Fair Trading consider that the reasons for the reduction in merger references include the link between merger activity and overall economic conditions, the development of the Office of Fair Trading's policy on undertakings, which has given parties more confidence in offering and dealing with undertakings in lieu, and the Office of Fair Trading's view that it is desirable in terms of speed and certainty of outcome to deal with cases at Phase 1 if it can be done without disproportionate effort.

**5.7** Since the Enterprise Act came into force there have been relatively few appeals – 12 in total – against Office of Fair Trading or Competition Commission merger decisions, all of which have been determined by the Competition Appeal Tribunal in under 12 months. In four of the 12 cases they were determined in less than one month.

### **Length of Competition Commission investigations**

**5.8** In terms of the performance against statutory time limits, the merger investigations carried out following referral by the Office of Fair Trading have all been completed within the 24-week statutory timeline (or within the subsequent 8-week extension period that can be granted). However, despite this, the speed of the merger regime process was ranked (in 2007) as being the second-worst of all countries surveyed in the then Department of Trade and Industry peer review (**Figure 13**).

### **Use of resources**

**5.9** The Chairman of the Competition Commission considers the existing system is not as effective as it could be, and does not necessarily lead to a good use of its resources. The lack of a compulsory pre-notification system means that some mergers get picked up later than he considers is desirable. In some cases, mergers reviewed by the Office of Fair Trading and Competition Commission have been completed (i.e. the companies have already merged) by the time of scrutiny and referral. Completed or partially-completed mergers can be significantly more complex to 'unscramble' and review, and more difficult when it comes to implementing effective remedies to address consumer detriment which may already have occurred.

**5.10** The UK's system of voluntary notification to the competition authorities of mergers is unlike most of the rest of Europe and the US, where compulsory pre-notification of larger mergers is required. However, a mandatory pre-notification system would require consideration to be given to the threshold for notification of a merger to the competition authorities (for example, to avoid covering lots of mergers that raise no competition issues), and also of the perceived concern that mandatory notification may cause a chilling effect on the economy (i.e. deterring mergers that would not be anti-competitive).

## Assessments of the regime

**5.11** Against this background, international observers' perceptions of the UK merger regime suggest that they consider it performs relatively well against other international comparators (Figure 13). The UK is rated second best for its technical competence and its independence from the political process.

**5.12** There have been a number of evaluations of merger decisions and outcomes. In 2005 an external evaluation of mergers cleared by the Competition Commission concluded that effective competition had resulted in all of the cases studied, with no evidence of substantial and/or sustained competition problems. And in 2008, an in-house evaluation of two merger prohibitions and one merger clearance found that the Competition Commission's decisions were sound, but recognised the challenges it faced to the extent that markets often 'move on' in directions that cannot always be fully anticipated.

**5.13** In addition, the Competition Commission calculated figures for annual consumer benefit for 2008-09 arising from the five mergers cases handled by the Competition Commission and the Office of Fair Trading as £313 million.

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### Figure 13

Rankings from the Department of Trade and Industry's Peer Review 2007

<b>Characteristic</b>	<b>International ranking out of 8 (where 1 is best score and 8 is worst)</b>
Technical competence in terms of economic analysis	2
Technical competence in terms of legal analysis	3
Technical competence of administrative staff	2
Clarity of procedures	4
Speed of decision-making	7
Minimal burden on business	4
Political independence	2
Ability of investigators to make independent, impartial recommendations	3
Resources available for caseload	4

*Source: Department for Business, Innovation and Skills*

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# Part Six

## Oversight, funding, and resources

**6.1** The oversight and funding of the bodies with competition powers are spread around government, meaning that no one department has oversight of the entire system. To function effectively as a system, and to meet the aims of the 2001 Competition White Paper cost effectively, it is important that there is an appropriate system wide view of resources and expertise. This part examines the oversight and governance arrangements for the bodies in the competition regime, the resources used in their competition activities, and how this is matched to the workflows. **Figure 14** lists all the main bodies, their funding streams and sponsor department.

**6.2** To coordinate matters relating to the Competition Act 1998, representatives of the competition bodies meet on a regular basis as the Concurrency Working Party. This group considers the practical working arrangements between the bodies; in order to provide a vehicle for the discussion of matters of common interest and the sharing of information where appropriate. The Department for Business, Innovation and Skills has also set up the Competition Forum<sup>23</sup> (a cross-Whitehall gathering of officials interested in competition issues) which meets on a regular basis.

23 The Forum is led by the Department for Business, Innovation and Skills, and the Office of Fair Trading.

**Figure 14**  
Funding and Sponsorship of Competition Authorities

	<b>Governance</b>	<b>Funding</b>
<b>Non-Ministerial Government Departments</b>		
Office of Fair Trading	Board Department for Business, Innovation and Skills	HM Treasury Fees
Office of the Gas and Electricity Markets	Board Department of Energy and Climate Change	HM Treasury Levies
Water Services Regulation Authority <sup>1</sup>	Board Department for Environment, Food and Rural Affairs	HM Treasury Levies
Office of Rail Regulation <sup>1</sup>	Board Department for Transport	HM Treasury Levies
<b>Public Corporations</b>		
Office of Communications	Board Department for Business, Innovation and Skills Department for Culture Media and Sport	Fees Department for Business, Innovation and Skills Department for Culture Media and Sport
Civil Aviation Authority	Board Department for Transport	Levies
<b>Non-Departmental Public Bodies</b>		
Competition Commission	Council Department for Business, Innovation and Skills	Department for Business, Innovation and Skills

Source: National Audit Office

**NOTE**

<sup>1</sup> Denotes Regulators in receipt of 'token vote' funding from HM Treasury (usually £1,000 per year). Boards are appointed by the Secretary of State of the department identified under 'Governance'.

**6.3** We gathered cost and resource information from all the bodies in the regime. Splitting out the costs relating purely to competition activity, we found that the whole regime costs some £27 million<sup>24</sup> annually (**Figure 15**), with spend on external advice of at least £8.6 million since 2005<sup>25</sup>. There are 372 staff in total operating the regime, 246 of whom have competition enforcement experience.

### Workflows in the competition regime

**6.4** The flow of work within and between the bodies in the regime has varied greatly over time, but has a direct impact on the cost efficiency of the system. This is because while one body may be busy, another may not. Activity levels within the organisations are largely a reflection of that particular body's assessment of the existence of problems in its sector, and in the Office of Communications' case specific duties under the EU framework and the Communications Act 2003. Workflows between the bodies in the system are largely driven by the amount of work referred by the Office of Fair Trading and the Regulators to the Competition Commission. This means that the Competition Commission relies on the Office of Fair Trading and the Regulators to select and refer appropriate cases and markets, creating a challenge for all bodies to make full use of the Commission's expertise.

**Figure 15**  
Resources across the UK competition regime

	<b>Totals</b>
Annual spend	£27m
Spend on external advice since 2005 <sup>1</sup>	£8.6m
Number of staff	372
Number of staff with experience of competition enforcement <sup>2</sup>	246
Number of loans/secondments since 2005 <sup>3</sup>	22

*Source: National Audit Office based on data provided by competition bodies and Regulators*

#### NOTES

- 1 See footnote 25 in this Part.
- 2 We asked the competition bodies and the Regulators to estimate the number of their staff who had experience of a substantial involvement in an investigation(s) using competition powers i.e. Article 101/Chapter 1 or Article 102/Chapter 2.
- 3 Not all the bodies keep complete data on secondments going back to 2005, so these numbers may be understated.

24 These costs cover the direct costs of Competition Act and Enterprise Act work. When overheads are included, the total increases significantly. These costs exclude the Office of Communications' work arising from the application of European law and other competition duties which involve an additional 89 full time equivalent staff.

25 Not all bodies had records going back to 2005 that were readily accessible or that would allow these types of costs to be identified without disproportionate cost, so this figure may be understated.

**6.5** **Figure 16** shows how the workflows in the regime impact on the Competition Commission. Since June 2007 there has been a reduction in the Competition Commission's workload resulting from a drop in new market references since 2007, and a low merger reference rate.

**6.6** The flexibility of the system to utilise staff resources where the work is, and to manage peaks and troughs at organisational level, is important in achieving cost efficiency.

**6.7** At the organisational level, the Regulators have relatively small competition teams; for example, the Office of Rail Regulation and the Water Services Regulation Authority each have around four people (**Figure 17** overleaf). Whilst the Regulators can draw in resources from other parts of their organisations on competition work, and can redeploy their own competition staff internally, they have to balance resourcing competition work with other objectives, obligations and priorities. This can constrain their ability to respond using competition powers.

**Figure 16**

The Competition Commission's overall caseload



Source: Office of Fair Trading/Competition Commission evaluation of the market investigations regime<sup>1</sup>

**NOTE**

<sup>1</sup> This caseload analysis excludes regulatory references and responding to remittals from the Competition Appeal Tribunal.

**6.8** At the system level, secondments can provide flexibility in resourcing the system, although the specialist skills required, in particular on competition enforcement, means that finding suitable candidates for secondment is not as straightforward as just seconding staff from another part of the Civil Service. We found seven staff have been seconded from the Competition Commission to the Office of Fair Trading to help manage the trough in the Competition Commission's workload in the last 12-18 months, with a further 11 secondments at other times (**Figure 18**). However, since 2005 there have been only four other loans or secondments in total around the competition regime. There is no system-wide view of resource use meaning that there is a risk that resource use is not optimised at a system level.

### Figure 17

Competition staff across the competition bodies and Regulators

Office of Fair Trading	Competition Commission	Office of Communications	Office of the Gas and Electricity Markets	Office of Rail Regulation	Water Services Regulation Authority	Total
265	78	21	Note 1	4	4	372

Source: National Audit Office based on data provided by competition bodies and Regulators

#### NOTE

1 The Office of the Gas and Electricity Markets handles enforcement cases on a project basis drawing in staff from across the organisation. A typical investigation would involve two members of the relevant division, a lawyer, and two members of the Enforcement and Competition Policy Team.

### Figure 18

Competition regime secondments, 2005 to 2009

Office of Fair Trading	Competition Commission	Office of Communications	Office of the Gas and Electricity Markets	Office of Rail Regulation	Water Services Regulation Authority	Total
3	18	0	1	0	0	22

Source: National Audit Office based on data provided by competition bodies and Regulators

#### NOTE

Not all bodies keep complete data on secondments going back to 2005, so these numbers may be understated.



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**Key concerns for debate**

- The various competition authorities and Regulators are overseen by a number of different bodies within government and have separately staffed competition functions. However, work flows unevenly around the competition system with the risk that resource use is sub-optimal. The arrangements for secondments and deployment of staff could be made more flexible to help optimise the use of resources and expertise around the system.
  - Some Regulators have small competition teams which could struggle to deal simultaneously with more than a very limited number of competition investigations. If a Regulator were to receive a strongly-evidenced complaint which it considered had a wider significance to the competition system, there is a risk that the regime as a whole would not be sufficiently flexible to resource it.
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