

**EVERSHEDS LLP: RESPONSE TO OFT CONSULTATION:
EXCEPTIONS TO THE DUTY TO REFER AND UNDERTAKINGS IN LIEU
PROPOSED CHANGES TO THE OFT GUIDANCE**

I. INTRODUCTION

1. Eversheds LLP welcomes the opportunity to respond to the above consultation. This Response is set out as follows:
 - II Markets Of Insufficient Importance (“De Minimis”)
 - III Responses To Specific OFT Questions
2. Where appropriate, our comments relating to the topics: mergers not sufficiently far advanced; relevant customer benefits; and undertakings in lieu are included in Section III of this Response.
3. This Response does not contain confidential information.

II MARKETS OF INSUFFICIENT IMPORTANCE (“DE MINIMIS”)

4. Eversheds LLP welcomes the OFT’s consultation on the exercise of its discretion not to refer mergers on the grounds that they concern markets of insufficient importance. Guidance is urgently needed because the OFT’s practice has developed significantly and appears to diverge from the standing guidance, *Exception to duty to refer: markets of insufficient importance (OFT 516b)*.
5. However, we consider that the draft guidance fails in its stated aim “to enhance predictability for companies considering acquisitions in relatively small markets” (paragraph 2.3). The draft guidance suffers from the following main flaws:
 - The guidance is overly complex and will not in practice facilitate self-assessment.
 - The views expressed are overly cautious.
 - The focus on a cost/benefit analysis is misplaced.
6. These failings are made more significant by the fact that the UK merger regime is arguably the most burdensome and expensive in Europe. The OFT is urged to reconsider the draft guidance with a view to identifying a “bright line” threshold that is simple to apply and gives both regulators and business greater certainty as to how the OFT will exercise its discretion under Sections 22(2)(a) and 23(2)(a) of the Enterprise Act (“EA”).

The guidance is too complex and does not facilitate self-assessment

7. The standing guidance states that:

"The OFT is generally likely to consider the affected market(s) to be of sufficient importance to justify a reference where their annual value in the UK, in aggregate, is more than £10 million Below the £10 million market size threshold, the OFT would generally consider the market to be of insufficient importance to justify a reference, subject to the caveats listed below."

8. The proposed revised guidance can be summarised as follows:

- Market size > £10 million - generally the OFT will not apply the exception but the exception may still apply if the market size marginally exceeds £10 million (paragraph 2.2).
- Market size £6 million - £10 million - the OFT will consider applying the exception but would be unlikely to do so above a market size of £6 million unless strong factors suggest that it should (paragraph 2.2).
- Market size £3 million - £6 million - the OFT will consider applying the exception (paragraph 2.2).
- Market size < £3 million - the OFT will generally apply the exception unless the "factual matrix" means it is appropriate to refer (paragraph 2.14).

9. The proposed revised guidance is more complex and introduces unnecessary additional thresholds at £3 million and £6 million and includes discretionary exceptions at each level. In so doing, it does not in practice enhance predictability of decision making or self-assessment - particularly for small companies who would often be those most likely to benefit from effective guidance.

10. The proposed guidance builds on the OFT's experience in various cases. However, it fails to offer a bright line test that could be used by parties in assessing mergers and complicates rather than simplifies the position. Given the OFT's experience to date it is disappointing that the OFT has not felt able to offer a more clear cut test. In practice, the complexity of the test may in fact increase costs for both companies and the OFT as small companies would be increasingly likely to seek Informal Advice.

The views expressed are overly cautious

11. In our view, the OFT should have the courage of its convictions and adopt a test that creates a genuine safe harbour below which it would exercise its discretion in all (or in all but the most exceptional) cases. In our view, the threshold

should be set at the original level of a market size of £10 million. Alternatively, if the OFT is not confident that this is the right level, it might reasonably set the threshold at a lower level with the possibility of revising it upwards once it has greater experience.

12. The OFT's timorous approach is in contrast to that adopted, for example, in Germany. Under the Act against Restraints of Competition ("ARC"), merger control is disapplied to mergers affecting a relevant market which has been in existence for five years and which has a total annual value of less than €15 million. The ARC test does not include the caveats and exceptions that the OFT guidance envisages and in practice has delivered a workable and predictable threshold for business and relieved the German authorities from the burden of unnecessarily reviewing small deals.

The focus on the cost/benefit analysis is misplaced

13. Sections 22(2)(a) and 33(2)(a) EA refer to the exception to the duty to refer applying where the market(s) are not of sufficient importance to justify a reference.
14. Paragraph 2.5 of the proposed guidance states that the purpose of the exception is to avoid references being made where the costs involved would be disproportionate to the size of the market(s) concerned.
15. The above language sensibly suggests that the exception should be applied by reference to the size of the markets concerned. Market size is readily quantifiable by both parties and the OFT and gives a simple and common sense test.
16. Unfortunately, the proposed guidance goes on to describe a "broad cost/benefit analysis" to be used in applying the OFT's discretion, taking into account public costs (but not the parties' costs); availability of undertakings in lieu; consumer harm; and deterrent effects. The inclusion of the latter two grounds, in particular, is unhelpful. Again, it adds complexity and makes it much harder for parties to self assess their mergers and departs from the simple test of importance of market contemplated in the Act.

Conclusion

17. In conclusion, whilst the revised guidance is well intentioned, it over-complicates and fails to enhance certainty for the OFT or the parties. The guidance proposes such a complex and subjective test that companies involved in mergers affecting small markets may find themselves increasingly availing themselves of the Informal Advice procedure (as foreseen by paragraph S2.60 et seq.). This outcome would involve parties and the OFT spending considerable time and resources analysing complex issues relating to the smallest of deals.

Accordingly, the OFT is strongly urged to operate a bright line test based on the size of the market that offers a genuine safe harbour which both the OFT and the parties are able to apply effectively. In our opinion, a market size of £10 million would be an appropriate threshold.

III RESPONSES TO SPECIFIC OFT QUESTIONS

Q1 Do you agree that assessing whether to exercise the "de minimis" discretion on the basis of a broadbrush cost/benefit approach is a reasonable approach to this discretion?

Whilst this approach might be considered "reasonable" it is not the best approach for the reasons give above. Both the OFT and parties would benefit from a simpler test based on market size.

Q2 Do you agree that the OFT should only take account of public - and not private - costs in considering the cost of a reference, given that it generally takes decisions based on a consumer - and not total - welfare basis?

If the OFT operates a cost benefit analysis, then the OFT should focus on consumer welfare. However, relevant costs should include not just the public costs but also private costs including, for example, costs of management resources, costs resulting from delays in the merger review process and the costs of the process itself.

Q3 Do you agree that the OFT's Dunfermline Press policy position with respect to the proportionality of a reference where undertakings in lieu are available is a reasonable one?

Yes.

Q4 Is it clear what the OFT means when it refers to undertakings in lieu being "in principle" available in the context of de minimis? If not, what further guidance would be useful?

Yes.

Q5 Do you agree that the OFT should take account deterrence when considering whether to apply its "de minimis" discretion? If so, how?

No. We think the benefits both to the OFT and the parties of a bright line test based purely on market size outweigh the benefits of including a deterrence element in the OFT's analysis. If the OFT wishes to add this additional complexity, the guidance should make clear that it would remove the safe harbour only in the most exceptional cases.

Q6 *Is it reasonable for the OFT in considering whether to apply a "deterrence multiplier" to have regard to the economic rationale behind a merger?*

Yes, but only in the most exceptional cases should deterrence be used to remove the safe harbour.

Q7 *The OFT states in its previous guidance that it might consider use of the exception less appropriate where a reference would have important precedent value, for example, because the case raises novel issues, so that an in-depth CC inquiry would provide guidance for the industry concerned. Do you consider that this caveat should be retained?*

No.

Q8 *Do you agree with the OFT's stated intention to use "de minimis" to reduce, where possible, the costs of a Phase I investigation?*

Yes this is of considerable benefit.

Q9 *Are there any other mechanisms other than those listed by which the OFT should use the "de minimis" discretion to reduce the burden of merger control?*

No.

Q10 *Are there any concerns about parties being willing to waive their procedural rights to an issues letter and issues meeting if the OFT would, in any event apply the "de minimis" exception?*

No.

Q11 *Is the right level of detail given in relation to how the OFT exercises its "de minimis" discretion? If more detail is required, in what areas should this be?*

As is evident from the comments above, we consider that the test formulated is much too complex and that the guidance is also too complex as a consequence.

Q12 *Do you believe there are any types of situation in which the OFT has not historically employed this exception but where it should do so going forward?*

No.

Q13 *Is the OFT applying the correct evidential standard in relation to consumer benefits?*

Yes.

Q14 *Do you agree with the OFT's explanation of the relationship between efficiencies that prevent a substantial lessening of competition from occurring and relevant*

customer benefits that outweigh and identify a substantial lessening of competition?

Yes.

Q15 Is it right to consider evidence on customer benefits on a sliding scale.

Yes.

Q16 Why have parties been unable to substantiate a customer benefits exception at Phase I under the Act to date?

It may just be that the right set of circumstances has not arisen. We would expect that the customer benefits exception would only ever be used rarely.

Q17 In what circumstances, if any, should the OFT be willing to accept a mitigatory remedy given that there remains a possibility of a reference to the CC?

Those specified in the draft guidance at paragraph 5.16.

Q18 Should the OFT be concerned about a risk of over-enforcement in terms of accepting undertakings in lieu (potentially requiring significant divestments), particularly given the level of the reference test?

No. It is up to the notifying party to take its own view on the undertakings to be offered and the benefits to it of avoiding a reference.

Q19 Should the OFT be prepared to allow parties to abandon/totally unwind a transaction through undertakings in lieu?

Yes. There is no benefit in unnecessarily forcing a purchaser on a completed transaction to go through a CC reference.

Q20 Do you agree that the proportionality of the divestment in the context of the wider transaction is irrelevant at the OFT stage?

Yes.

Q21 Do you agree that the OFT does not have the power to accept undertakings in lieu from a purchaser of divestment assets?

Yes.

Q22 In what circumstances, if any, should the OFT seek informal ongoing behavioural comments from a purchaser of divestment assets or a divestment business?

We would not be in favour of use of such informal commitments that could not ultimately be enforced.

Q23 *Do you agree that the OFT's use of the upfront buyer mechanism provides a proportionate means of addressing divestment risk? Are there any risks around this mechanism that might be addressed?*

The upfront buyer mechanism provides a proportionate solution.

Eversheds LLP
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