

Annexe H

Competition Act 1998 and Enterprise Act 2002
considerations

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ANNEXE H

COMPETITION ACT 1998 AND ENTERPRISE ACT 2002 CONSIDERATIONS

Introduction

1.1. As outlined in Chapter 1, when the OFT launched this study possible outcomes included investigation under the Competition Act 1998 (CA98) or a market investigation reference to the Competition Commission under the Enterprise Act 2002 (EA02). This Annexe outlines why we consider neither option to be appropriate at this time:

- Section A: Competition Act investigation
- Section B: Competition Commission Reference

Section A: COMPETITION ACT INVESTIGATION

Reasonable grounds for suspecting an infringement

- 1.2. Several stakeholders have requested that the OFT undertake investigations under CA98. Broadly these requests have been on the basis that limiting the number of wholesalers appointed by a manufacturer (where as part of a DTP scheme or as a variant to the traditional wholesale model) results in the prevention, restriction or distortion of competition at the wholesale level. These stakeholders have argued that either (i) the manufacturers and wholesalers that are party to these arrangements have entered into agreements that are in breach of Chapter I of CA98 and/or (ii) that the manufacturers' refusal to supply competing wholesalers represents an abuse of a dominant position under Chapter II of CA98.

- 1.3. It is important to distinguish between effects that arise from exclusivity or appointing a limited number of wholesalers and those that arise from DTP itself. We have made recommendations to Government to deal with concerns arising from DTP, and we do not believe that the concerns that arise from arrangements which limit the number of distributors raise sufficient concerns to justify action under CA98, when considered against the OFT's prioritisation criteria. Given this, we do not need to take a view on whether there are reasonable grounds for suspecting an infringement of CA98 in respect of the Pfizer agreement, or similar agreements, relating to the distribution of medicines. This does not however rule out the possibility that reasonable grounds may be found in the future on these or other arrangements, or the possibility that the OFT might take action under CA98 in the future.

Prioritisation

- 1.4. The arrangements in question concern healthcare, which is one of the sectors where the OFT will continue to work to increase its understanding of the competition and consumer issues that exist. However, it is not clear that enforcement action under CA98 is the best use of OFT resources in this case, because a number of the concerns attributed to these arrangements relate to DTP schemes themselves, rather than to limiting the number of appointed wholesalers/LSPs, and are best addressed via the recommendations to Government outlined in Chapter 6.

- 1.5. We have identified two areas of concern relating to the distribution changes. Firstly, there is a significant risk that DTP schemes will increase the costs to the NHS, and secondly we consider there to be a high risk that the distribution changes will result in a reduction in the service to patients.
- 1.6. **Costs to DH:** We consider that DTP is likely to result in lower discounts to pharmacies, and higher NHS costs. Under DTP, manufacturers set the discount to pharmacies and at this level there is no discount convention that is equivalent to the 12.5 per cent discount generally applied to sales to wholesalers. The same concern arises whether a DTP manufacturer appoints all wholesalers or only one. We consider that the risk of these cost increases is most appropriately dealt with by making recommendations to Government about the PPRS scheme (see Chapter 6).
- 1.7. **Service to patients:** There are two main concerns here. The first relates to whether the reduction of the number of wholesalers used to distribute a manufacturer's medicines give rise to competition concerns. We consider that where a single wholesaler is appointed, that wholesaler is unlikely to have sufficient incentive to provide a high level of service to pharmacies. Where more than one wholesaler is appointed, this will provide for some competition and therefore better service standards (see Chapter 4 for more detail).
- 1.8. The second relates to the incentive manufacturers have to require high service levels from appointed wholesalers. Under the traditional wholesale model, service level is a significant element of wholesalers' competition for pharmacy accounts. Under DTP, manufacturers specify the service level they require, and their incentive to provide a high level of service does not coincide with the pharmacies' demand for a high level of service. Therefore it is possible that manufacturers will seek to specify lower levels of service for their medicines (see Chapter 4 for more information).
- 1.9. Of these concerns, only the first effect relates to appointing an exclusive wholesaler. The potential impact on consumers of this is not sufficient, on its own, to warrant an investigation under CA98 at this time. We do consider however that the widespread appointment of exclusive wholesalers has the potential to result in competition problems in future. For this reason, we have highlighted the benefits of making wholesaler appointments that preserve effective competition to manufacturers. Were a number of manufacturers to

appoint an exclusive wholesaler, the OFT may wish to intervene in this sector in future (see Chapter 6).

- 1.10. The second concern relates to DTP and is relevant irrespective of the number of wholesalers appointed by a manufacturer. To address these concerns, we have made recommendations to Government (see Chapter 6).

SECTION B: COMPETITION COMMISSION REFERENCE

- 1.11. A reference to the Competition Commission under EA02 was another possible outcome of this market study if we found reasonable grounds for suspecting that any feature, or combination of features, of the market prevents, restricts or distorts competition.

- 1.12. Although we have identified concerns arising from changes to distribution, we have chosen not to refer the market to the Competition Commission at this time. This is because the concerns we have identified are best dealt with by changes to the PPRS. We therefore consider it more appropriate to recommend changes to the PPRS to Government than to refer the market to the Competition Commission.