

# Agenda

Advancing economics in business

## Merging the merger authorities

**No two countries are the same when it comes to the institutional design of their regulatory and competition authorities. The UK government is considering merging its two highly rated competition bodies, the Office of Fair Trading and the Competition Commission. Oxera's response to the government's consultation on the matter is provided below**

Competition and regulatory authorities around the world vary enormously in their size, shape, independence and powers. In some countries, the competition authority is simply the competition authority. In the UK, the Office of Fair Trading (OFT) also has a separate consumer protection role. In the Netherlands, the NMa is the sectoral regulator for transport and energy as well as the competition authority.

Recently, there have been moves in some countries to reconfigure these institutions. In the Netherlands, the NMa will merge in 2013 with the Dutch Post and Telecommunications Authority (OPTA) and the Dutch Consumer Authority. In the UK, the postal regulator, Postcomm, will merge with the much larger electronic communications regulator, Ofcom.

An example of another proposed institutional merger—between the UK's two main competition bodies, the OFT and the Competition Commission (CC)—is the focus of this article. The UK government department for Business, Innovation and Skills (BIS) recently completed a public consultation on whether the OFT and CC should be merged to form a new Competition and Markets Authority (CMA).<sup>1</sup>

Under the current UK competition regime, the OFT has jurisdiction over cases that are brought under the UK Competition Act 1998 and Articles 101 and 102 of the European Treaty, such as anti-competitive agreements and abuse of dominance. For mergers, the OFT is the phase 1 competition authority, and refers cases to the CC for in-depth investigation if it has concerns that cannot be easily remedied. For market inquiries, the OFT carries out an initial study and then decides whether to refer the market to the CC or to adopt one of a number of alternative outcomes (for example, close the inquiry, or agree a set of remedies with the parties concerned). Businesses can appeal the

decisions of the OFT and CC to the Competition Appeal Tribunal (CAT).

The BIS consultation proposes streamlining the process of dealing with mergers and market investigations by merging the OFT and CC. It also suggests a range of options for how the merged entity might operate; these include extending the use of the CC's current approach, whereby decisions are taken by a panel of members, or even moving to a prosecutorial system in which the CMA would present cases before a court rather than being the decision-maker.

So, would an OFT/CC merger create value for the shareholders—ie, UK taxpayers—and would it lead to clear customer benefits? In order to add some economic rigour to the debate, this article turns the tables and subjects the proposed merger to the standards of merger control that the OFT and CC would normally apply to cases on which they adjudicate.

### A merger review

The proposed 'transaction' is primarily a vertical merger. The CC does not and cannot initiate cases itself, but must instead have cases referred to it by the OFT (or the sector regulators acting under their concurrent powers<sup>2</sup>). The OFT is therefore the primary provider of work to the CC.

The current structure of vertical separation has advantages, but also some downsides and inefficiencies. While the CC has many high-quality resources available to it at both panel and staff level, the usage of these resources is somewhat unpredictable, given that the CC cannot initiate cases and therefore cannot manage its staff utilisation. By moving to a vertically integrated structure, there may be scope to:

- reduce demands for information from parties by avoiding the duplication of data requests, as can sometimes occur under the current system;
- enhance staff understanding of cases by retaining the same project team for phase 1 and phase 2, which would make meetings at phase 1 more valuable in cases that are highly likely to be referred to phase 2;
- reduce the overall duration of market studies and investigations.

As with vertical mergers in general, whether such inefficiencies will be eliminated in practice depends on the detailed design and implementation of the new structure.

There are also some quasi-horizontal aspects to the merger. Some direct rivalry between institutions would be lost under the proposals. In particular, there is currently a form of informal ‘benchmark competition’ between the OFT and the CC, reflected in the various rankings of international competition agencies. While the ‘relevant market’ for this benchmark competition includes competition agencies worldwide, the OFT and CC probably currently see each other as their closest rivals. This horizontal rivalry can be healthy. As emphasised by BIS in its consultation document (para 1.4), both the OFT and the CC have consistently been ranked among the leading competition authorities in the world by *Global Competition Review* (GCR) and other studies.<sup>3</sup>

Yet another part of the merger is of a ‘conglomerate’ nature. The CC deals with mergers and market investigations only, not with Competition Act cases (while the OFT does not deal with regulatory references and appeals). Indeed, further merger efficiencies may arise in this regard. For example, the expertise of the competition economists and financial experts at the CC can be readily applied to abuse and agreement cases (not being able to work on such cases is somewhat inefficient, and perhaps also unsatisfactory, from the perspective of the CC staff). There also seems to be scope for greater alignment of the decision-making structures across Competition Act cases and market investigations (see comments below).

BIS is minded to retain the ‘divestments’ made by (or forced upon) the OFT when the Competition Act was enacted in 1998—ie, the concurrent powers awarded to the sector regulators. Indeed, such powers have since been, or are being, extended to cover postal services and health. The case for or against concurrency is complex, and would require more in-depth debate and analysis than is currently provided in the BIS document (Chapter 7). Meanwhile, some of BIS’s suggestions that point towards greater involvement of the new authority in those sectors seem to have some merit, even if concurrency is retained (an example being the

European Competition Network model<sup>4</sup>). It is important to avoid conflicting decisions and achieve better coordination between sector regulators and competition authorities, both for better decision-making and for providing greater legal certainty to regulated companies.

Lastly, as with mergers of any nature, there are issues surrounding brand and culture. As noted above, the OFT and the CC both have well-established international names. A merger between two big brands inevitably destroys some brand value if one of the brands disappears. Sometimes one brand is kept, but that may be difficult if the merger is between equals, as may be said to be the case here. Brand advisers might decide on a new name that sounds as familiar and authoritative as the previous ones (footnote 8 of the consultation document notes that the ‘Competition and Markets Authority’ is a working title for the new entity at this stage).

In any merger it is important that the best cultural aspects are taken from the merging parties. In this case, for example, one of the strengths of the CC is that it has a culture of openness (at both staff and panel level), and is generally willing to submit to analysis and review of much of its work during investigations (both formally and more informally). The OFT also has this to some extent, but its formal and informal processes have fewer built-in mechanisms for interaction with the parties. Openness to scrutiny will form a key part of the high-quality decisions to be made by the new authority.

## A competition system in which evidence is properly assessed

One of the most important elements of the competition regime as a whole is to ensure that economic evidence and the economic merits of a case receive the attention that they deserve. This is not a plea to increase the use of economists in these cases; rather, the aim is to improve the quality of the competition regime. Weighing up economic evidence in the legal context is crucial to reaching well-reasoned decisions.

When considering timelines for cases of all types, it is important that parties are given sufficient time to fully review and respond to the competition authority’s economic analysis. This can be time-consuming task in instances where the competition authority has produced complex analysis. Time also needs to be built into case timescales to allow parties to submit their own primary analysis, which can be helpful in enabling competition authorities to reach well-reasoned conclusions. This implies that, if timescales are to be shortened as is currently suggested, this should not be at the sole expense of the time allowed for parties to make submissions to the authorities; these timelines are already tight under the current structure.

In Oxera's experience, the most effective legal cases—from the perspectives of the parties and the decision-maker—are those where the legal advisers, the business people and the economists present an integrated submission that reflects both the business reality and sound economic reasoning. This may then be complemented by separate, probably more technical, economic submissions containing empirical evidence. Competition authorities and courts must take a view on how much weight to attach to this evidence. Economic evidence needs to be presented in such a way that it allows for a proper peer review by the economists at the competition authority or on the other side of the dispute. In this regard, the various guidance documents on best practice for submissions of technical economic analyses that have been issued in recent years by competition authorities, including those documents provided by the European Commission and the CC, are a welcome development.<sup>5</sup>

The CC panel structure lends itself to a thorough weighing of the evidence (factual, financial and economic), with a panel of lawyers, economists and business people. The panel hearings offer the opportunity to 'leave no stone unturned', and to ask questions of parties and their advisers from both a public policy and a technical perspective. Indeed, as part of its ongoing emphasis on quality and independence, Oxera's internal project debriefs routinely ask the question: 'Would the project director/project manager be happy to present this piece of work in front of a CC panel?'

The CC panel structure has its merits, and the BIS consultation document seems to want to retain such a structure within the new organisation for market investigations and mergers. In principle, a thorough review of the evidence by a panel could also benefit Competition Act 1998 cases. There is no inherent difference between these types of case in terms of the need to assess the economic merits and arguments on both sides.

An alternative suggested by BIS (option 3 in Chapter 5) is the move towards a more prosecutorial system, whereby a competition authority has to argue its case before a court or tribunal, and this court or tribunal makes the judgment. There are several costs and benefits of such a regime, and weighing these up is a complex exercise. We focus on one of the benefits below: the way in which the system takes into account economic and other evidence.

Economic evidence is rarely black and white in the context of any Competition Act case that is sufficiently interesting to be considered in detail by the competition authorities. This makes the task of a competition authority conducting such a case under an

administrative regime difficult: individuals from the same organisation must first collate evidence, then act as a prosecutor by pulling this evidence together and putting it to the parties, and finally act as a judge by deciding on the merits of the case. Even with an independent person from outside the case team (but within the competition authority) acting as the final decision-maker, it is difficult to prevent biases slipping into such a system.

There may therefore be merit in a move to a prosecutorial system for Competition Act cases. By removing decision-making power from the OFT/CMA, this would ensure independence of outcome and remove any conflicts of interest that the decision-maker might have. Furthermore, such a system would increase incentives for the authority, and the parties, to conduct high-quality work throughout, and to be clear and transparent about their arguments and conclusions. Any errors, omissions or incoherent logic would be subject to independent scrutiny. In light of this, a solution might be to convert the CAT from an appellate body to a court of first instance, to which the OFT (or the CMA) would bring its prosecutorial case. This would preserve the expertise that exists within the CAT, would not necessitate the creation of a new body, and so would be likely to limit the costs and disruption of such a change to the competition regime.

By the same token, the 'new administrative approach' referred to in the BIS consultation document (option 2 in Chapter 5) might not be an appropriate solution. Even if an independent tribunal *within* the CMA were set up, there is a risk that, by continually dealing with the staff of the same competition authority, these independent individuals would, over time, come to identify with the CMA. Moreover, this approach does not allow the same degree of scrutiny and review of the evidence.

In a prosecutorial system, economic experts could be subject to the same rules as currently applied in the English courts (and CAT). Part 35 of the Civil Procedure Rules determines that experts have a duty to help the court on matters within their expertise. In Oxera's experience, this provides a powerful incentive to the expert to carry out the analysis objectively and reliably. Judges tend to rapidly dismiss the evidence of an expert who does not appear to want to be helpful to the court. There have been numerous judgments in which courts have explicitly stated that they found an economic expert's evidence to be credible, persuasive or authoritative, and that they felt they could rely on the expert. Equally, courts have indicated where there were some doubts in this respect. In addition, the experts from both sides of a dispute are normally expected to hold discussions and produce a joint statement setting out the issues on which they agree

and disagree (and their reasons). Together with the duty to the court, this requirement on experts to narrow the issues in dispute can be a powerful mechanism to help courts understand the economics of a case. Finally, an economist involved in court proceedings faces the prospect of cross-examination by a barrister representing the other side. Subjecting the new CMA to such rigour and discipline would be beneficial to the quality of decision-making.

## Concluding comment

There is no one optimal model of institutional design for competition regimes, and a myriad of structures will continue to exist across the world. This in itself is

useful, since it allows for comparative studies and learning from best practice between countries.

Several of the changes recommended by BIS, and some of the ideas discussed above, could enhance the UK competition regime and allow it to maintain its position among the leading regimes in the world for years to come.

It seems that there are indeed clear potential benefits to shareholders and customers from the proposed merger between the OFT and the CC. Whether they are realised depends on the government's appetite for making real changes to the way the merged entity operates.

<sup>1</sup> Department for Business Innovation and Skills (2011), 'A Competition Regime for Growth: A Consultation on Options for Reform', March.

<sup>2</sup> The regulators of the rail, water, energy, telecoms and air traffic control sectors have powers alongside the competition authorities to apply the competition rules. These are known as 'concurrent powers'.

<sup>3</sup> In the 2011 GCR rating, the CC was rated among the top four 'elite' agencies, together with the European Commission's DG Competition, the US Department of Justice, and the US Federal Trade Commission; the OFT was in joint fifth place and rated 'very good'.

<sup>4</sup> Through the European Competition Network, the European Commission and the national competition authorities in all EU Member States cooperate with each other. For example, they inform each other of proposed decisions and take on board comments from the other competition authorities. See [http://ec.europa.eu/competition/ecn/index\\_en.html](http://ec.europa.eu/competition/ecn/index_en.html).

<sup>5</sup> European Commission (2010), 'Best Practices for the Submission of Economic Evidence and Data Collection in Cases Concerning the Application of Articles 101 and 102 TFEU and in Merger Cases', January; and Competition Commission (2009), 'Suggested Best Practice for Submission of Technical Economic Analysis from Parties to the Competition Commission', February.

If you have any questions regarding the issues raised in this article, please contact the editor, Dr Gunnar Niels: tel +44 (0) 1865 253 000 or email [g\\_niels@oxera.com](mailto:g_niels@oxera.com)

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