PUBLIC CONSULTATION ON THE DRAFT COMPETITION BILL

SUBMISSION TO THE MINISTRY OF TRADE AND INDUSTRY

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1. **EXECUTIVE SUMMARY**

1.1 Introduction

1.1.1 Wong Partnership ("WP") would like to thank the Ministry of Trade and Industry ("MTI") for the opportunity to comment on the proposed competition bill ("Bill"). WP's comments are set out below.

1.1.2 WP welcomes the introduction of the Bill and applauds the MTI for its efforts to create a pro-enterprise environment. WP believes that the Bill will play a pivotal role in attracting investment into Singapore. On its part, WP is encouraged by this new development in the law as we anticipate that the Singapore economy will benefit from the policies that the Bill intends to implement.

1.2 WP's General Views

1.2.1 In this feedback, unless otherwise stated, references to section numbers refer to those in the Bill. References to captioned terms follow those defined in the Bill.

1.2.2 The following set out the key areas of the Bill which WP would like to comment upon:

(a) General comments, applicable to the entire Bill

(i) Differences between United Kingdom ("UK") /European Community ("EC") Competition regime and the proposed Singapore Competition regime;

(ii) The lack of a framework for market definition in the Bill;

(iii) Concerns as to the possible retrospective effect of the Bill (for instance at section 34(5) and section 54(1));

(iv) Queries on the wide powers of the Competition Commission ("CC"), including the power to investigate and to adjudicate. In this regard, WP hopes that comprehensive provisions on the scope of the CC's powers, and how the CC intends to use them in practice, will be set out in guidelines, on which there should be full and open consultation; and

(v) The role of the court.

(b) The section 34 prohibition

(i) Clarifications on the definition of "Undertakings", as provided in section 2 in relation to agreements affected by the section 34 prohibition;

(ii) Guidance on what "Appreciable Adverse Effect" on markets in Singapore means, and preferably, including the term "Appreciable

Adverse Effect" in the Bill (with regard to the section 34 prohibition);

(iii) Amending the examples of anti-competitive behaviour in section 34(2);

(iv) Provide more clarity on the legal consequence upon a breach of the section 34 prohibition, and in particular, to consider allowing the doctrine of severance to apply to section 34(3);

(v) Inclusion of a legal defence for the section 34 prohibition instead of a regime requiring undertakings to continually seek exemptions from the CC; and

(vi) Benefits in excluding vertical agreements from the section 34 prohibition.

(c) The section 47 prohibition

(i) Inclusion of a definition of "dominance", together with the defence of objective justification as well as clarification on the scope of section 47(3);

(ii) Proposed removal of section 47(2)(c) in light of the EC's review of Article 82 and EC jurisprudence on this issue;

(iii) Practical difficulties in having undertakings continually seek guidance from the CC with respect to their conduct.

(d) The section 54 prohibition

(i) Support for a voluntary merger regime;

(ii) Inclusion of clear turnover thresholds to provide legal certainty as to whether a transaction is sufficiently material as to merit notification;

(iii) Sanctions for mergers to be limited to entities established in Singapore; and

(iv) Any notification and clearance decision to cover ancillary restraints as well as the transaction itself.

1.2.3 Finally, WP looks forward to queries the MTI may have arising from WP's feedback. WP also awaits the opportunity to comment on any draft guidelines that the MTI may wish to develop in relation to the implementation of the Act.

2. STATEMENT OF INTEREST

WP is a law firm with an established commercial practice.

The draft Bill potentially affects many of our clients' businesses in Singapore. In fact, since the publication of the draft Bill, several of our clients (comprising MNCs as well as

local businesses) have approached us with queries, comments and/or other feedback on the Bill.

We have since had the opportunity of reviewing the provisions of the Bill and have done a brief study of comparative competition law regimes in other countries.

We take this opportunity to give our comments on the Bill, which is based upon our own understanding of the provisions in the Bill, and feedback which we have received from our clients in relation to their concerns on the provision of the Bill.

3. GENERAL COMMENTS

3.1 Differences between UK / EC Competition regime and the proposed Singapore Competition regime

3.1.1 WP notes that a substantial portion of the Bill is based on the UK Competition Act 1998. Sections 34 and 47 are very similar to the UK Chapter I and II prohibitions, whilst our section 54 prohibition is largely based on Part 3 of the UK Enterprise Act 2002.

3.1.2 However, there is a fundamental difference between the UK and Singaporean legislation, which must be taken into account when drafting the Bill. When the Competition Act 1998 was brought into force in the UK, it deliberately included section 60, which imports the jurisprudence of the EC courts in Luxembourg applying EC law. There was therefore no need to define key competition law principles and definitions on the face of the UK's Competition Act 1998 itself, because section 60 enables the 36 years' worth of EC legal jurisprudence to be included in the UK Act.

3.1.3 Singapore's Bill cannot include the extensive body of existing EC and UK competition law jurisprudence in the same way. Without the incorporation of this jurisprudence, our Bill should therefore be as precisely drafted as possible, to prevent any uncertainties, in order that undertakings know how they should order their business activities. Two examples are the definition of "undertaking" for the purposes of the section 34 prohibition, and the definition of "appreciable adverse effect". These and other examples will be explored in more detail below.

3.1.4 Whilst the CC may be able to issue guidelines, WP respectfully submits that guidelines cannot replace the statute, in particular since the guidelines are not binding on either the CC or the courts.

3.2 Lack of a framework for Market Definition

3.2.1 The importance of market definition cannot be understated.

3.2.2 In the UK, the Office of Fair Trading ("OFT") intends to introduce specific guidelines (currently at the public consultation stage) on this issue alone[1]. Many pertinent points relating to the significance of market definition are contained in the OFT's draft guidelines, and WP seeks only to highlight the more significant ones (in relation to the Singapore economy / draft Bill) for the MTI's consideration. The OFT's guidelines on market definition (OFT 403) are attached at Annex A.

3.2.3 Market definition is an integral part of establishing whether or not particular agreements or conduct fall within the scope of the section 34 prohibition and/or the section 47 prohibition.

3.2.4 WP understands that the law intends to only focus on anti-competitive agreements or conduct which will have an "appreciable adverse effect on markets in Singapore".

3.2.5 To meaningfully apply this appreciability test, a definition of the relevant market would be required. It is only after the definition is set out, that one can determine whether such an agreement and/or conduct will have the prohibited effect on competition within a particular market.

3.2.6 Separate and distinct from providing a framework for competition analysis, an appropriately defined relevant market may also provide information that will allow an investigation to be closed at an early stage.

3.2.7 For instance, under section 34, where an agreement involves undertakings whose combined share of the relevant market is low, the agreement is unlikely to raise competition concerns, unless it contains practices prohibited in section 34(2).

3.2.8 Likewise, for an analysis under section 47, undertakings with low market shares will usually not possess market power individually. Thus, it may be possible to complete investigations relating to such undertakings at a very early stage.

3.2.9 Given the importance of defining the markets appropriately, WP considers that the Bill should set out the approach and principles that the CC will follow in defining the "relevant" market.

3.2.10 This can be done by reference to international best practice and the latest economic thinking of peer group competition authorities, with a view to precluding the distortion of international trade through the application of competition principles which might be at odds with those applied in other major trading blocs around the world. However, it should be made clear that these international practices and principles need to be applied in the specific (and different) context of the Singapore economy and the individual circumstances of the particular market in Singapore, rather than just importing foreign concepts wholesale.

[1] OFT's draft competition law guideline for consultation published on April 2004 in relation to market definition, OFT 403.

3.2.11 WP submits that the inclusion of such an approach and principles would give comfort to international businesses that the assessment of markets for competition law purposes across the world will be governed by a broadly consistent approach through adherence to established principles of international best practice.

3.2.12 WP also submits that guidelines on market definition, along the lines of those issued by an established competition authority, for instance the UK's OFT, should be issued by the CC following appropriate consultation, in order to set out in detail the CC's intended methodology for assessing market definition.

3.3 Retrospective effect of the Bill

3.3.1 The prohibitions in the draft Bill appear to have a retrospective effect:

> Section 34(5) - "Subsection (1) applies to agreements, decisions and concerted practices implemented **before**, on or after the appointed day" (Emphasis Added)
>
> Section 54(1) - "Mergers that **have resulted**, or may be expected to result, in a substantial lessening of competition within any market in Singapore for goods or services are prohibited." (Emphasis Added)

3.3.2 The effect of the wording suggests that agreements and mergers entered into prior to the Act coming into force may be subject to these provisions. Such a retrospective effect may impose too great a burden on companies and create uncertainty which is not conducive for businesses.

3.3.3 In addition, WP notes that the UK's Competition Act 1998, on which the draft Bill is largely based, did not have retrospective effect when it came into force in March 2000. This accorded with the principle of legitimate expectation for businesses. Similarly, both UK and EC merger law is prospective, rather than retrospective, its entire rationale being based on regulating future rather than past conduct.

3.3.4 WP hopes that the MTI can clarify the scope of these 2 clauses, particularly whether they are in fact intended to have retrospective effect.

3.3.5 If the 2 clauses above are not intended to be retrospective, WP suggests that the relevant clauses be amended to reflect this. If however the MTI intends for the Bill to have retrospective effect, WP submits that only future (which may include continuing) conduct that infringes any of the prohibitions in the Bill be caught, and not all of that undertaking's past conduct.

3.4 Competition Commission's Powers

3.4.1 WP notes that the CC has both investigatory and adjudicatory powers (see sections 62, 68). WP submits that this approach may place too heavy a reliance on the CC and its resources, especially given the wide-ranging effect of the Bill.

3.4.2 Further, there may also be concerns among businesses as to transparency, given that a single body is both prosecutor and judge. WP therefore suggests that these 2 functions be clearly delineated within the CC, and that such demarcation be specifically set out in the Bill, to avoid any potential for conflicts of interests. The allocation of investigatory and enforcement powers to separate departments within the CC would enable the enforcement division to act as a "fresh pair of eyes" when reviewing the evidence gathered by the investigation division, which would be fairer for the undertakings concerned and more transparent.

3.4.3 WP further hopes that comprehensive provisions on the scope of the CC's powers, and instances where they would act, be incorporated within the Bill and/or in guidelines following appropriate consultation. In the UK, the OFT is consulting on draft guidelines on its powers of investigation (OFT 404, April 2004) and on its enforcement powers (OFT 407, April 2004). The draft guidelines provide extensive guidance on procedure and how the OFT intends to use its powers in practice. OFT's guidelines on its powers of investigation (OFT 404) and on its enforcement powers (OFT 407) are attached at Annex B and Annex C respectively.

3.4.4 WP submits that the CC should do the same in respect of its powers, to address outstanding questions raised by the Bill including:

(a) whether or not the privilege against self-incrimination will apply in the context of the CC's investigations[2];

(b) whether the CC will have the right to seal premises that it has entered for the purposes of an investigation;

(c) whether the parties will have the opportunity to make oral as well as written representations under section 68(1)(b)(ii);

(d) internal targets for the time taken to complete investigations; and

(e) staffing provisions; etc.

3.4.5 In relation to section 71, regarding appeals on the CC's decisions, WP asks that the Bill clarifies whether an appeal to the Competition Appeal Board will be a full appeal on the merits, or whether it will merely be an assessment of the "reasonableness" of the decision, along the lines of judicial review. WP hopes that the former approach will be adopted, as in the UK, in order to better safeguard the rights of the parties concerned.

3.5 Role of the courts

3.5.1 WP feels it is important to further clarify the role of the courts.

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[2] The legislature can direct application of the rules of evidence contained in the Evidence Act (Cap 97) to apply to proceedings before tribunals. Apart from section 66 of the Bill incorporating litigation and legal professional privilege, there appears to be no express provisions to incorporate the formal rules of evidence set out in the Evidence Act.

3.5.2 Section 75 currently provides that the rights of private action only arise after the CC has reached a prior decision that the act or conduct in question is in breach of section 34 or 47 or 54. Section 75 is however silent on whether a breach of these sections can be raised as a defence when a party is sued (on grounds unrelated to the provisions in the Bill). For instance, in the event Party A sues Party B, for a breach of an agreement between them, can Party B argue that the agreement is void because it contravenes section 34?

3.5.3 WP would submit that Party B should not be allowed to raise such a defence, except where there has been a prior decision by the CC. To require the court to rule on such a defence would give rise to a situation where 2 separate bodies, i.e. the CC and the courts, are given the power to decide on matters relating to the Bill. This could potentially give rise to confusion arising from different treatments of the same issue by the 2 bodies. Further, as competition matters are a specialised field, WP submits that decisions relating to the same should be undertaken by a specialist body, i.e. the CC. The court's role can be limited to its appellate powers, as contemplated for rights of action under section 75 of the Bill.

3.5.4 In other words, a defendant should not be allowed to raise a breach of sections 34, 47 or 54 as a defence, unless it has a prior decision of the CC to that effect.

3.5.5 Alternatively, in circumstances where a defendant raises a breach of sections 34, 47 or 54 as a defence, a court can be given the express power to stay the proceedings, and refer the matter of whether there has been in fact a breach of the aforesaid sections to the CC (or a specialist competition court, should one be established in the future).

4. THE SECTION 34 PROHIBITION

4.1 Clarifications on "Undertakings" falling within the section 34 prohibition

4.1.1 The term "undertaking" is defined in section 2 as follows:

> "undertaking" means any person, being an individual, an association, a body corporate or an unincorporated body of persons, capable of carrying on commercial or economic activities relating to goods or services."

4.1.2 The definition suggests that all separate legal entities are caught, regardless of whether such undertakings are related or otherwise.

4.1.3 The only exception to this relates to the section 54 prohibition. Under section 54(7), undertakings directly or indirectly under the control of the same undertaking are excluded from the section 54 prohibition.

4.1.4 The express exemption of “related” undertakings under the section 54 prohibition further supports an interpretation that the section 34 prohibition would apply to agreements between related entities.

4.1.5 WP submits that in respect of the section 34 prohibition, related undertakings should be excluded.

4.1.6 Under the present draft, an agreement between a parent and its subsidiary or between two companies which are under the control of a third would be subject to the section 34 prohibition.

4.1.7 This is notwithstanding the fact that the subsidiary has no real freedom to determine its course of action on the market, and enjoys no economic independence. WP believes that it is not the intention of the bill to prohibit such agreements, between related undertakings, and would thus ask that the definition of "undertakings" be revisited.

4.1.8 In this regard, WP highlights to the MTI the approach of the UK and EC courts, when addressing this issue.

4.1.9 WP understands that in the UK and EC, whilst they do not have a definition for "undertakings" (either under the Competition Act 1988 or the Treaty), EC case law has held that the undertakings which form a single economic unit are exempted from the Chapter I prohibition (in the UK) and the Article 81 prohibition (in the EC Treaty)[3].

4.1.10 We note that the UK does not define the term "undertaking" in its Competition Act 1998, because the case law from the EC courts is imported into the Act by virtue of section 60.

4.1.11 In the UK, the OFT's Guidelines provide that:

> "…an agreement between a parent and its subsidiary company, or between two companies which are under the control of a third, will not be agreements between undertakings if the subsidiary has no real freedom to determine its course of action on the market and, although having a separate legal entity, enjoys no economic independence."

4.1.12 WP believes that with regards to this issue, the UK / EC experience should be followed, and we would submit that the position in the UK / EC, i.e. that the equivalent to the section 34 prohibition is inapplicable to undertakings that form a single economic unit, should likewise be adopted in Singapore.

4.1.13 This exception should be specifically stated in the Bill, as the UK position is not binding on our local courts.

4.1.14 Further, as far as WP is aware, the EC law doctrine of single economic unit has not been applied in Singapore before and no other legislation has interpreted "undertakings" is such form. To avoid uncertainty on this issue, Parliament's intention should be made clear in the proposed Bill.

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[3] Like section 34 of the Bill, Chapter 1 of the UK Competition Act 1988 and Article 81 prohibitions in the EC Treaty relate to anti-competitive agreements. The relevant EC case in which "undertaking" was first defined as a single economic unit, and therefore not to include intra-group transactions, is Case 22/71 *Beguelin Import v GL Import Export* [1971] ECR 949; [1972] CMLR 81.

4.2 Guidance on what "Appreciable Adverse Effect" means

4.2.1 Paragraph 6b of the Consultation Paper to the Draft Bill states that:

"Instead of attempting to catch all forms of anti-competitive agreements or conduct in all markets, focus will be placed on anti-competitive agreements or conduct that will have an ***appreciable adverse effect*** on markets in Singapore." (Emphasis Added)

4.2.2 However, this requirement that the impact should be appreciable is not found in the draft Bill. WP submits that the legislation should provide for this requirement of appreciability.

4.2.3 We understand that the UK's Competition Act 1998 does not provide for appreciability in its legislation. Again, this is because the case law of the EC courts, where the appreciability test is established, is imported into the UK's Competition Act 1998 by virtue of section 60.

4.2.4 As noted above, the position is different for Singapore, which cannot import the EC jurisprudence in the same way. It is therefore important that the "appreciable adverse effect" is set out on the face of the Bill.

4.2.5 The MTI has already made it clear that the intention is to focus only on agreements or conduct that will have an appreciable adverse effect.

4.2.6 We would submit that the inclusion in the Bill of the "**appreciable adverse effect**" test would afford greater certainty and comfort to the business community at large. In addition, it would avoid a flood of concerned undertakings making submissions for exemption (even though their agreements/conduct do not have an appreciable adverse effect) out of an abundance of caution, which would give rise to unnecessary work for the CC.

4.3 Examples of anti-competitive behaviour in Section 34(2)

4.3.1 Section 34(2) includes the following as the final two examples of agreements, decisions or practices which may fall within the section 34(1) prohibition:

"(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; or

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts."

4.3.2 WP considers that these two examples go beyond what is necessary for the effective enforcement of competition law. Although they were originally included under Article 81 of the EC Treaty when it was first drawn up in 1957, and have remained there ever since, in practice they are rarely, if ever, the subject of enforcement under the UK / EC equivalents of the section 34

prohibition. Instead, such behaviour is usually considered under the equivalents of the section 47 prohibition.

4.3.3 WP therefore believes that these subsections should be removed from the Bill in order to ensure that Singapore's Competition Act is in keeping with up-to-date international competition practices.

4.4 Legal effect of breach of Section 34 prohibition

4.4.1 WP queries the legal status of an agreement should there be an inadvertent breach of the section 34 prohibition, particularly if section 34 is deemed to have retrospective effect.

4.4.2 Section 34(3) of the draft Bill provides that any agreement or decision, which is prohibited by subsection (1), is void.

4.4.3 The first concern that arises over the term "void" is whether an agreement which was in force prior to the Act coming into force, but continuing to be in force thereafter, will be considered "void ab initio". WP submits that the agreement should (at most) only be void from the date that the agreement infringes the section 34 prohibition, and that this date must be after the date that the Act comes into force.[4] If not, the Act would have retrospective effect, which, as stated above, would create uncertainty for the parties and run counter to the principle of legitimate expectation.

4.4.4 WP's second concern is that the effect of making an entire agreement void would have serious consequences for agreements of which only part is affected by the anti-competitive conduct.

4.4.5 Under EC law, only the offending provision of the agreement is unlawful. The agreement as a whole will only be void where that provision is not severable from the remaining terms of the agreement. It is up to the proper law of the agreement to determine the effect on the agreement as a whole of the relevant provision(s) being void.[5] This important principle is imported into the UK's Competition Act 1998 by virtue of section 60, and therefore also applies to UK competition law.

4.4.6 We would therefore suggest that a specific provision be included to state that only portions of the agreement that contain the anti-competitive elements are void. In other words, WP hopes that the Bill will expressly provide that the Act will not affect the validity or enforceability of an agreement otherwise than in relation to portions that fall foul of the section 34 and 47 prohibitions.

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[4] This is in accordance with the UK judgment of *Passmore v Morland plc & ors (*[1999] 3 All ER 1005, [1999] 1 CMLR 1129, [1999] EuLR 501), where it was held that the nullity imposed by Article 81(2) of the EC Treaty has the same temporaneous or transient effect as the prohibition in Article 81(1) (the EC equivalent of the section 34 Prohibition).

[5] *Société Technique Miniere v Maschinenbau Ulm GmbH*, Case 56/65 [1966] ECR at page 250.

4.4.7 This appears to be the position adopted by the Bill, as section 69 seems (albeit it appears to contradict the use of the term "void") to give the CC the power to sever offensive portions of an agreement found to be in breach the section 34 prohibition. If this is in fact the case, WP would ask that the Bill clarifies this.

4.4.8 Thirdly, having regard to commercial realities, we would additionally suggest a separate clause stating that should the result of the severance result in a substantial or material variation of the contract or fundamentally differs from the parties' original intention, the entire contract, in such an instance, would then be void.

4.4.9 Fourthly, we are also aware that for a period of time, there was some uncertainty as to whether a contract that was void under the equivalent UK provision was also illegal[6]. The repercussions for such void contracts being illegal would be that money paid under such a contract would be irrecoverable. The EC courts have since held that claims for damages under Article 81 of the EC Treaty are not prevented by the principle of illegality,[7] and again this jurisprudence is imported into the UK's Competition Act 1998 because of section 60. WP would therefore suggest that the Bill itself specifically addresses this issue of whether contracts that which are void under the draft Bill are also illegal.

4.4.10 Finally, WP would seek clarification as to whether the section 34 prohibition is an absolute prohibition i.e. any agreements or decisions once prohibited pursuant to section 34(1) shall thereafter be automatically void, or whether it is a prohibition which arises when, and continues for so long as (and only for so long as), it is needed in order to prevent, restrict or distort competition within Singapore, which is the stated objective of section 34(1).

4.4.11 The UK / EC has adopted the latter position[8]. WP suggests the MTI consider whether it would like to adopt a similar position, since the mischief of the Bill is to address anti competitive behaviour, which would not be the case once an agreement (although originally prohibited and therefore void) ceases to be in breach of the section 34 prohibition.

4.4.12 Should the UK / EC position be adopted, WP also seeks clarification as to whether the corollary principle of transient voidness, i.e. that an agreement may, in its lifetime, drift into and out of unlawfulness under the EC equivalent of the section 34 prohibition, would be applicable in Singapore.

4.5 Legal Defence to section 34 instead of an exemption procedure

4.5.1 WP understands that the UK has adopted a legal defence to their equivalent of the section 34 prohibition. In other words, an agreement that satisfies certain provisions (for instance those set out in section 41) would not be prohibited, and

[6] *Crehan v. Courage Limited* [1999] 3 All ER 1005

[7] Case C-453/99, *Courage v Crehan* [2001] ECR I-6297.

[8] *Passmore v Morland plc & ors* [1999] 3 All ER 1005

no prior decision to that effect is required. WP is of the view that providing for a legal defence, instead of an exemption procedure (as envisaged in section 41) would probably be advantageous, as it obviates the need to repeatedly approach the CC for guidance and/or exemptions before entering into agreements. Additionally, adopting the UK position in this regard would also be in line with the "guiding principles" of the Bill set out in the Consultation Paper of keeping regulatory costs to a minimum.

4.6 Vertical Agreements

4.6.1 We believe it is beneficial to the economy that the Bill seeks, as a first instance, to exclude all vertical agreements from the section 34 prohibition. This position reflects the reality that vertical agreements rarely raise substantial competition concerns, and that most vertical agreements are benign and need not be exposed to scrutiny.

4.6.2 The only instances where vertical agreements may potentially give rise to competition concerns would be when one or more of the parties to the agreement possess market power on the relevant market or the agreement forms part of a network of similar agreements.

4.6.3 Even in such situations, the MTI may wish to consider that the agreement should still be excluded from the section 34 prohibition, as the section 47 prohibition would adequately mitigate the fear that an undertaking with market power could act anti-competitively under such situations.

4.6.4 In the present draft Bill, section 8(1) of the Third Schedule allows the Minister to order that specified vertical agreements are not excluded from the section 34 prohibition.

4.6.5 Such a scope for wide exception gives rise to uncertainty.

4.6.6 Undertakings are not able to know whether their current vertical agreements would subsequently be the subject matter of the exception, in which case, their current vertical agreements would be regarded as void.

4.6.7 Given the above, we would request the MTI to consider (by making the necessary amendments to the Bill) that in relation to the section 34 prohibition, all vertical agreements are excluded.

5. THE SECTION 47 PROHIBITION

5.1 Clarifications on the definition of "dominance"

5.1.1 WP also requests further guidance on the scope of the section 47.

5.1.2 In relation to this section, we feel it is important to distinguish market leadership / market strength from dominance (which in any event is per se not objectionable, unless there has been an abuse of that dominant position).

5.1.3 Put simply, a market leader is (inter alia) one who knows what the consumer wants, one who consistently innovates its products, one whom other competitors seek to follow. Dominance and market leadership are thus different concepts, although the two are not mutually exclusive. Market leadership, being customer oriented, is pro-competition, and therefore poses no anti-competitive concerns.

5.1.4 All businesses would have an interest in knowing how market dominance would be determined under the provisions of the Bill. Particularly, it would provide comfort to leading industry players if they could be assured that their position as market leaders would not be to their detriment, in the context of the new competition regime.

5.1.5 WP submits that it is important for a definition of "dominance" to be included in the Bill itself. This is especially important since, as noted above, Singapore cannot import the extensive body of EC jurisprudence into its Bill unlike section 60 in the UK's Competition Act 1998. A clear definition of dominance is needed in order to give legal certainty to businesses, and to ensure consistent application of the law (subject of course to its application in the appropriate local context) across the international trading community.

5.1.6 WP therefore suggests that the draft Bill define dominance by reference to factors such as the economic strength enjoyed by an undertaking, which such undertaking enjoys to the extent that it is able to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors and customers and ultimately of consumers.[9]

5.1.7 Secondly, consideration should be given to not stipulating a market share threshold as the criterion for defining "dominance" under section 47 as this is only one factor to be taken into account in the assessment of whether an undertaking is dominant. Other factors ought also to be considered, such as the position of other undertakings operating in the same market, barriers to entry, and how the undertaking's market shares have changed over time.

5.1.8 Although the guidelines could set a threshold, over which there would be a presumption of dominance (as is done in some other jurisdictions)[10], WP submits that this trend is potentially restrictive and places too much importance on market share as an indicator of dominance, which may give a misleading impression of the market, especially in emerging and dynamic markets where the market share has not been held long and/or is likely to be subject to change over time as a result of competitive pressure.

5.1.9 WP therefore submits that the guidelines for assessing dominance should specifically set out the range of other relevant factors to be taken into account

[9] As first stated by the European Court of Justice in *United Brands v Commission*, Case 27/76 [1987] ECR 207, [1978] 1 CMLR 239.

[10] For example, the EC courts have held that there is a presumption of dominance where an undertaking has a market share of 50% (*AKZO v Chemie*, Case C-62/86, [1991] ECR I-3359).

(such as barriers to entry, characteristics of the relevant market, profile of other competitors, retailer or buyer power etc).

5.1.10 Thirdly, in EC and UK competition law, in order to distinguish abusive behaviour caught by the Article 82 / Chapter II prohibition from legitimate behaviour outside it, the European Commission and Community courts have established the fundamental principle of "objective justification" (imported into the UK Competition Act 1998 by section 60). The principles of objective justification and proportionality are firmly part of the Article 82 / Chapter II analysis.

5.1.11 WP therefore submits that similar principles should be included in the Bill. Introducing a new subsection can achieve this.

5.1.12 The new sub-section can have reference to factors such as the principle of proportionality and whether or not the conduct of the undertaking or undertakings concerned can be objectively justified. WP further submits that the defence of objective justification should include, but is not limited to, legitimate conduct on behalf of an undertaking or undertakings to protect its intellectual property rights and other property rights, as well as considerations of public health, safety and security.

5.1.13 The possibility of raising an objective justification in relation to property rights is appropriate given that it is rare for measures taken by an undertaking to safeguard such rights to be sufficiently exploitative as to constitute an "abuse".

5.1.14 Fourthly, we also seek clarification on the interpretation of section 47(3), which defines "dominant position" as dominant "within Singapore or elsewhere. As far as we are aware, the UK / EC competition law regimes do not have a similar concept of extra territoriality, and the Bill thus may be perceived to be out of step with international best practice. That said, WP appreciates that there may be policy reasons (e.g. the size of the Singapore market) why an extra territorial definition is adopted.

5.1.15 Given the inclusion of the phase "or elsewhere" in section 47(3), and in light of the fact that such a definition is not common in other competition regimes, WP suggests that the MTI set out clear guidelines on how the phrase "or elsewhere" will be interpreted, in order that businesses are aware of the basis upon which dominance will be determined.

5.2 List of Potential Abuses

5.2.1 Section 47(2) sets out a non-exhaustive list of abuses. The last two examples are as follows:

"(c): applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; or

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of the contracts".

5.2.2 The European Commission is currently reviewing the application of Article 82 (abuse of a dominant position), particularly in relation to discriminatory pricing and loyalty rebates. Economic thinking has progressed in such a way that often price discrimination is deemed to be pro-competitive on today's economy, as the OFT's guidelines on assessment of conduct show.[11]

5.2.3 Likewise, the example set out in subsection (d) above is also very rarely relied upon.

5.2.4 In light of the suspect status of these historical categories of abuse, and the possible reforms to Article 82 / Chapter II that will be carried out once the EC's internal review of it is complete, WP submits that it would be unhelpful for the Singapore Competition Act to bind itself to the examples in section 47(2)(c) and (d).

5.2.5 WP therefore suggests that, for the sake of future-proofing the legislation and keeping options so as to ensure consistency with international best practice, these subsections should be removed.

5.3 Practical difficulties

5.3.1 WP is also concerned about the regulatory costs and inconvenience which would arise over the present section 49.

5.3.2 Section 49 allows a person who considers that his conduct may infringe the section 47 prohibition to request the CC to review such conduct, and to apply for guidance.

5.3.3 First, it is unclear whether section 49(1) includes applications by third parties in respect of the allegedly abusive conduct of others, or is restricted solely to parties that are carrying out the conduct in question. WP submits it may be beneficial to restrict such applications to persons with a real (economic or legal) interest in the proceedings, to prevent a multitude of (frivolous) applications by third parties, and thereby unnecessarily clogging up the system.

5.3.4 Secondly, insofar as section 49(1) applies to the undertaking or undertakings carrying out the conduct in question, WP submits that it may be unrealistic to expect an undertaking that may be considered "dominant" to request official clearance for a business plan, practice or agreement. Doing so would increase

[11] OFT draft guidance on assessment of conduct, April 2004, OFT 414. See, for example, section 3.3: "Price discrimination occurs frequently and in a range of industries, including industries where competition is effective. It is a generic term that covers many specific types of pricing behaviour that can be either good for consumers or anti-competitive. Therefore, it is not necessarily the case that price discrimination by a dominant undertaking is an abuse".

the costs of doing business, and also potentially causes losses to the undertaking, since there might be delays caused by the application for guidance.

5.3.5 The practical effectiveness of such a provision would thus be open to question.

5.3.6 The consequence may be that undertakings that are really abusing their dominant positions keep silent about their conduct, whereas others, who may choose to act more cautiously, continually inundate the CC with their requests for guidance. Given the burden that such requests could impose on the CC, the MTI may wish to reconsider the notification provisions in sections 50 and 51.

6. SECTION 54 PROHIBITION

6.1 Ambit of the section 54 prohibition

6.1.1 WP welcomes the creation of a voluntary merger regime, giving the parties the freedom to make their own judgment regarding notification.

6.1.2 WP believes that it is essential for minimum jurisdictional thresholds to be included in the Bill, in order to give businesses (especially the international business community) legal certainty as to whether or not it is appropriate to notify the transaction. At the moment, the provisions are very wide, appearing to capture all transactions of any scale. The absence of defined thresholds could give rise to notifications of even very small transactions that are unlikely to meet the substantive test (of substantial lessening of competition), leading to a unnecessarily heavy workload for the CC.

6.1.3 WP would therefore suggest that the MTI considers including clear turnover thresholds as the appropriate jurisdictional criteria for Singapore. Turnover is the clearest and simplest means of creating a materiality threshold. Normally an undertaking's turnover in Singapore would be used; however, given the importance of exports to Singapore's economy, it may be appropriate for the turnover test to include export-based turnover. An alternative, and possibly more appropriate, threshold, given the presence of numerous MNCs in the open Singapore economy, could be one relating to incremental turnovers. In other words a merger that does not result in an increased turnover of a certain amount or percentage of current turnovers of the companies involved would automatically fall outside the scope of the section 54 prohibition. WP recognises that there are other tests, such as assets-based tests and market share- based tests. However the former is often complicated and less relevant to Singapore's economy whilst the latter gives rise to market definition issues, and therefore may deter parties from notifying.

6.1.4 The Bill should also make it clear that enforcement directions under section 69(2)(c) for infringement of the section 54 prohibition may only be made against an entity established within the jurisdiction. This principle is consistent with the situation in the EC, regarding the territorial jurisdiction of the European Commission, and in the UK, regarding the enforcement powers of the OFT and the (UK) Competition Commission. This position is also consistent

with section 69(4) which provides that, in relation to the fixing of financial penalty, only the turnover of the business of the undertaking in Singapore is considered.

6.1.5 It is particularly important to make this clear because, in the case of foreign to foreign mergers in Singapore, if orders were to be made against the foreign companies, it would be impossible in practice for the CC to enforce them in Singapore as there would be no means of implementing the enforcement, unless the companies had subsidiaries in Singapore.

6.1.6 WP also submits that it would be helpful for the Bill to state that any notification and clearance decision shall be deemed to cover ancillary restraints within the transaction documents, in order to give the parties legal certainty as to the status of such provisions.

6.1.7 Ancillary restraints are restrictive clauses whose presence is commercially essential to a particular transaction, and may include for example non-compete clauses or clauses protecting intellectual property rights. WP suggests that ancillary restraints should be defined in the Bill as being restraints that are "directly related and necessary" to the transaction, in accordance with EC law. This would reduce the burden on the CC who would not have to rule separately on the transaction documents.

7. CONCLUSION

The provisions of the draft Bill and the approach embodied in the consultation paper is positive towards the creation of a practical competition regime within Singapore, which will ultimately benefit the Singapore economy. WP believes that the Bill will no doubt achieve its intended purpose of creating "greater productivity gains and more efficient resource allocation".

WP is pleased to support the MTI's efforts to "enhance the efficient functioning of markets in Singapore and strengthen (her) microeconomic competitiveness", and look forward to participating in further refinements of the Bill as appropriate.

ANNEXURE A

OFFICE OF FAIR TRADING

Market definition

Draft competition law guideline for consultation

April 2004

OFT403a

Articles 81 and 82 of the EC Treaty and the Competition Act 1998 are applied and enforced in the United Kingdom by the Office of Fair Trading (the OFT). In relation to the regulated sectors these provisions are applied and enforced, concurrently with the OFT, by the regulators for communications matters, gas, electricity, water and sewerage, railway and air traffic services (under section 54 and schedule 10 of the Competition Act) 1998 (the Regulators). Throughout the guidelines, references to the OFT should be taken to include the Regulators in relation to their respective industries, unless otherwise specified.

The following are Regulators:

- the Office of Communications (OFCOM)
- the Gas and Electricity Markets Authority (OFGEM)
- the Northern Ireland Authority for Energy Regulation (OFREG NI)
- the Director General of Water Services (OFWAT)
- the Rail Regulator[1] (ORR), and
- the Civil Aviation Authority (CAA).

This guideline provides general advice and information about the application and enforcement by the OFT of Articles 81 and 82 of the EC Treaty and the Chapter I and Chapter II prohibitions contained in the Competition Act 1998. It is intended to explain these provisions to those who are likely to be affected by them and to indicate how the OFT expects them to operate. Further information on how the OFT has applied and enforced competition law in particular cases may be found in the OFT's decisions, as available on its website from time to time.

This guideline is not a substitute for the EC Treaty nor for regulations made and notices provided under it. Neither is this guideline a substitute for the Competition Act 1998 and the regulations and orders made under it. It should be read in conjunction with these legal instruments, Community case law and United Kingdom case law. The guideline contains a discussion of the relevant principles of Community law. It should not be seen as a substitute for or as a definitive interpretation of Community law. Anyone in doubt about how they may be affected by the EC Treaty and the Competition Act 1998 should seek legal advice.

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[1] This will change to the Office of Rail Regulation on 5 July, 2004.

CONTENTS

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1 INTRODUCTION

1.1 The EC Treaty[2] and the Competition Act 1998 (the Act) both prohibit agreements[3] which prevent, restrict or distort competition and conduct which constitutes abuse of a dominant position. EC Regulation 1/2003 (the Modernisation Regulation)[4] allows national competition authorities of the Member States (NCAs) and the courts of the Member States to apply and enforce Articles 81 and 82 of the EC Treaty (Article 81 and Article 82 respectively). The Act gives the OFT powers to enforce both the Chapter I and Chapter II prohibitions of the Act and Article 81 and Article 82. A more detailed explanation of the Modernisation Regulation is set out in the competition law guideline *Modernisation* (OFT442).

1.2 This guideline follows a similar approach to the European Commission's *Notice on market definition*.[5] This guideline provides a conceptual framework within which evidence on market definition can be organised. It also discusses practical issues that may arise in market definition. The OFT will not follow mechanically every step described below in every case. Instead, the OFT will look at evidence that is reasonably attainable and relevant to the case in question.[6]

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[2] The Treaty of Rome, establishing the European Community, as consolidated by the Treaty of Amsterdam.

[3] References in this guideline to 'agreements' should, unless otherwise stated or the context demands it, be taken to include decisions by associations of undertakings (see footnote 8 below) and concerted practices.

[4] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (OJ L1, 4.1.03, p 1).

[5] European Commission *Notice on the definition of the relevant market for the purposes of Community competition law* (OJ C372, 9.12.97, p 5). A similar approach is also used in the US Department of Justice and Federal Trade Commission *Horizontal Merger Guidelines*, revised 1992.

[6] While this guideline is specific to Articles 81 and Article 82 and the Act, the OFT will generally use the same approach to market definition in other areas of casework, including mergers and market investigation references. In this regard, it should be noted that the appropriate market definition can differ according to the specific facts of each case. Part 5 of this guideline gives more details.

2 MARKET DEFINITION

The purpose of market definition

2.1 Market definition is not an end in itself but a key step in identifying the competitive constraints acting on a supplier of a given product or service. Market definition provides a framework for competition analysis. For example, market shares can be calculated only after the market has been defined and, when considering the potential for new entry, it is necessary to identify the market that might be entered. Market definition is usually the first step in the assessment of market power.

2.2 Therefore, market definition is important in the process of establishing whether or not particular agreements or conduct fall within the scope of the competition rules:

- Article 81 and section 2(1) of the Act (**the Chapter I prohibition**) apply only to agreements which have as their object or effect an 'appreciable' prevention, restriction or distortion of competition (see the competition law guideline *Article 81 and the Chapter I prohibition* (OFT401)). The appreciability test usually requires definition of a relevant market and demonstration that the agreement would have an appreciable effect on competition within that market,[7] and
- Article 82 and section 18(1) of the Act (**the Chapter II prohibition**) apply only to dominant undertakings.[8] The OFT would not consider an undertaking to be dominant unless that undertaking had substantial

[7] An exception is where agreements have as their object the prevention, restriction or distortion of competition. In these cases, market definition is not necessarily a pre-requisite for finding an infringement: see Case T-62/98 Volkswagen AG v Commission [2000] ECR II-2707 at paragraphs 230 to 232. The relevant market would, however, need to be defined in order to determine the 'relevant turnover' of undertakings for the purpose of assessing the amount of any penalties (see the OFT's *Guidance as to the appropriate amount of a penalty* (OFT423)).

[8] The term 'undertaking' is not defined in the EC Treaty or the Act but its meaning has been set out in Community law. It covers any natural or legal person engaged in economic activity, regardless of its legal status and the way in which it is financed. It includes companies, firms, businesses, partnerships, individuals operating as sole traders, agricultural cooperatives, associations of undertakings (e.g. trade associations), non profit making organisations and (in some circumstances) public entities that offer goods or services on a given market. For further details, see the competition law guidelines *The major provisions* (OFT400) and *Article 81 and the Chapter I prohibition* (OFT401).

market power. Market definition is usually the first step in assessing whether an undertaking has substantial market power.

2.3 In addition to its value in providing a framework for competition analysis, an appropriately defined relevant market may provide information that allows an investigation to be closed at an early stage. For analysis under Article 81 and/or the Chapter I prohibition, where an agreement involves undertakings whose combined share of the relevant market is low, the agreement is unlikely to raise competition concerns unless it contains price fixing, market sharing or bid rigging restrictions.[9] Market definition is also important when assessing whether an undertaking's market share is below market share thresholds set out in certain block exemptions.

2.4 For analysis under Article 82 and/or the Chapter II prohibition, undertakings with low market shares will usually not possess market power individually. Therefore, an investigation of an individual undertaking whose market share is low can normally be closed at an early stage.[10]

The hypothetical monopolist test

2.5 The process of defining a market typically begins by establishing the closest substitutes to the product[11] (or group of products) that is the focus of the investigation. These substitute products are the most immediate competitive constraints on the behaviour of the undertaking supplying the product in question. In order to establish which products are 'close enough' substitutes to be in the **relevant market**, a conceptual framework known as the hypothetical monopolist test (the test) is usually employed.

2.6 Before describing the test in detail, it should be emphasised that defining a market in strict accordance with the test's assumptions is rarely possible. Even if the test described below could be conducted precisely, the relevant market is, in practice, no more than an appropriate frame of

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[9] See the competition law guideline *Article 81 and the Chapter I prohibition* (OFT401).
[10] See the competition law guidelines *Article 82 and the Chapter II prohibition* (OFT402) and *Assessment of market power* (OFT415).
[11] The focus of the investigation may be a product or a service. The term 'product' is used for convenience and should be interpreted throughout this guideline to mean good, service or property right.

reference for analysis of the competitive effects. Nevertheless, the conceptual framework of the hypothetical monopolist test is important as it provides a structure within which evidence on market definition can be gathered and analysed.

2.7 In essence the test seeks to establish the smallest product group (and geographical area) such that a hypothetical monopolist controlling that product group (in that area) could profitably sustain 'supra competitive' prices, i.e. prices that are at least a small but significant amount above competitive levels. That product group (and area) is usually the relevant market.

2.8 If, for example, a hypothetical monopolist over a candidate product group could not profitably sustain supra competitive prices, then the candidate product group would be too narrow to be a relevant market. If, on the other hand, a hypothetical monopolist over a subset of a candidate product group could profitably sustain supra competitive prices, then the relevant market would usually be narrower than the candidate product group.

2.9 The steps in applying this approach are as follows. We start by considering a hypothetical monopolist of the **focal product** (i.e. the product under investigation[12]) which operates in a **focal area** (i.e. an area under investigation in which the focal product is sold). We assume the hypothetical monopolist supplies no other products and sells in no other areas.

2.10 We then ask whether it would be profitable for the hypothetical monopolist to sustain the price of the focal product a small but significant amount (e.g. 5 to 10 ten per cent[13]) above competitive levels.[14] If the answer to this question is 'yes', the test is complete. The

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[12] Where there is more than one product under investigation, the test will usually be applied separately for each of the products.

[13] The OFT will normally consider a price 5 to 10 per cent above competitive levels to be 'small but significant'. However, this is only as an indicative range. If a price sustained 5 to 10 per cent above competitive levels would not be profitable but a higher price would be, a hypothetical monopolist could profitably sustain prices significantly above competitive levels and so the test is complete.

[14] When carrying out the test, we assume that the hypothetical monopolist is not subject to economic regulation that would affect its pricing behaviour and that the prices of products

product and area under the hypothetical monopolist's control is (usually) the relevant market.

2.11 If the answer to this question is 'no', this is typically because a sufficiently large number of customers would switch some of their purchases to other substitute products (or areas).[15] In this case, we assume further that the hypothetical monopolist controls both the focal product **and** its closest substitute.[16] We then repeat the process, but this time in relation to the larger set of products (or areas) under the hypothetical monopolist's control.

2.12 As before, we ask whether it would be profitable to sustain prices 5 to 10 per cent above competitive levels. If so, the test is complete. The relevant market is (usually) the focal product and its closest substitute. If not, we assume the hypothetical monopolist also controls the second closest substitute to the focal product and repeat the process once more. We continue expanding the product group in this way (i.e. by adding in the next best substitute) until we have found a group of products (or areas) for which it is profitable for the hypothetical monopolist to sustain prices 5 to 10 per cent above competitive levels.[17]

2.13 When the test is complete for the first time, the relevant market has usually been defined. However, occasionally it will be appropriate to

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outside of the hypothetical monopolist's control are held constant at their competitive levels. However, while not considered as part of the test, the issues of regulation and the pricing strategies of competitors would be considered as part of the overall competitive assessment.

[15] Sometimes the pricing strategy would not be profitable because of responses by other suppliers – this is known as supply side substitution and is discussed in Parts 3 and 4.

[16] The best substitute to the focal product could be another product sold in the same area or the focal product sold in a different area.

[17] Although the test discussed here refers to a hypothetical monopolist, it should be noted that an undertaking with less than 100 per cent of a relevant market may nevertheless have market power. For example, suppose the market has been defined such that a hypothetical monopolist would profitably sustain prices at, say, 10 per cent above competitive levels. First, since market power is a matter of degree, this leaves sufficient room for an undertaking with less than 100 per cent of the market to exercise market power by sustaining prices above competitive levels, even if that undertaking would not increase prices by as much as a hypothetical monopolist. Second, an undertaking with less than 100 per cent market share may have the ability to weaken any competition that it faces and thereby consolidate its market power even further. Third, undertakings in the market may dampen competition by co-ordinating their behaviour. In the extreme, if they colluded perfectly, a group of undertakings could behave as if they were a hypothetical monopolist. These issues should be considered as part of the assessment of market power. See the competition law guideline *Assessment of market power* (OFT415).

define the relevant market to be wider than the narrowest product group (or area) that passes the test (see, for example, the discussion of supply side substitution in Parts 3 and 4).

Practical issues

2.14 In practice, defining a market requires balancing various types of evidence and the exercise of judgement. However, it is not an end in itself. Where there is strong evidence that the relevant market is one of a few plausible market definitions, and the competitive assessment is shown to be largely unaltered by which one of these market definitions is adopted, it may not be necessary to define the market uniquely.

2.15 A market definition should normally contain two dimensions: a **product** and **geographic area.**[18] It is often practical to define the relevant product market first and only then to define the relevant geographic market. Parts 3 and 4 below discuss some of the issues that may arise when defining product and geographic markets and applying the principles set out above.

2.16 Part 5 discusses further practical issues such as market definition when prices may already exceed competitive levels. It also describes how the relevant market should be defined according to the facts and competition issues of each case. Part 6 discusses market definition in the context of after markets.

[18] Time is a third dimension that sometimes applies, see Part 5.

3 THE PRODUCT MARKET

The demand side

3.1 This part discusses some of the practical issues that need to be addressed when defining the relevant product market.

3.2 As described above in Part 2, the market definition process usually starts by looking at a relatively narrow potential definition. This would normally be one (or more) of the products which two parties to an agreement both produce, or one (or more) of the products which are the subject of a complaint about conduct, i.e. the focal product (or focal group of products). Previous experience and common sense will normally indicate the narrowest potential market definition, which will be taken as the starting point for the analysis.

3.3 As set out in Part 2, the next question is whether a hypothetical monopolist of the focal product could profitably sustain prices a small but significant amount above competitive levels. The price increase must be large enough that a response from customers is reasonably likely, but not so large that the price rise would inevitably lead to a substantial shift in demand, and so lead to markets being defined so widely that market shares convey no meaningful information on market power. The OFT will normally consider a price 5 to 10 per cent above competitive levels to be 'small but significant'.[19]

3.4 Following the price rise, customers may switch some of their purchases from the focal product to other substitute products (**demand side substitution**). It is not necessary for all customers, or even the majority, to switch. The important factor is whether the volume of purchases likely to be switched is large enough to prevent a hypothetical monopolist profitably sustaining prices 5 to 10 per cent above competitive levels.[20]

3.5 Substitute products do not have to be identical to be included in the same market. For example, in its report on *Matches and Disposable*

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[19] See Part 5 for a discussion of whether the current price is a reasonable proxy for the competitive price.

[20] The customers most likely to switch are sometimes called 'marginal' customers. Where a relatively high proportion of marginal customers purchase a product, a sustained 5 to 10 per cent price rise above competitive levels is less likely to be profitable.

Lighters[21], the then Monopolies and Mergers Commission included matches and disposable lighters in the same market because customers viewed them as close substitutes. Similarly, the products' prices do not have to be identical. For example, if two products perform the same purpose, but one is of a higher price and quality, they might be included in the same market. The question is whether the price of one sufficiently constrains the price of the other. Although one is of a lower quality, customers might still switch to this product if the price of the more expensive product rose such that they no longer felt that the higher quality justified the price differential.

3.6 The important issue is whether the undertaking could **sustain** prices sufficiently above competitive levels. Customers may take time to respond to a sustained rise in the price of the focal product. As a rough rule of thumb, if substitution would take longer than one year, the products to which customers eventually switched would not be included in the same market as the focal product. Products to which customers would switch within a year without incurring significant switching costs[22] are more likely to be included in the relevant market. However, the relevant time period in which to assess switching behaviour may be significantly shorter than one year, for example in industries where transactions are made very frequently. A case by case analysis of switching is therefore appropriate.

3.7 Evidence on substitution from a number of different sources may be considered. Although the information used will vary from case to case and will be considered in the round[23] the following evidence and issues are often likely to be important:

- Evidence from the undertakings active in the market and their commercial strategies may be useful. For example, company documents may indicate which products the undertakings under

[21] Cm 1854, 1992.
[22] From a customer's point of view, switching costs can be defined as the real or perceived costs that are incurred when changing supplier but which are not incurred by remaining with the current supplier.
[23] Aberdeen Journals Limited v. Office of Fair Trading [2003] CAT 11 (Aberdeen Journals (No. 2)) at [128].

investigation believe to be the closest substitute to their own products. Company documents such as internal communications, public statements, studies on consumer preferences or business plans may provide other useful evidence.[24]

- Customers and competitors will often be interviewed. In particular, customers can sometimes be asked directly how they would react to a hypothetical price rise, although because of the hypothetical nature of the question, answers may need to be treated with a degree of caution. Survey evidence might also provide information on customer preferences that would help to assess substitutability: for example, evidence on how customers rank particular products, whether and to what extent brand loyalty exists, and which characteristics of products are the most important to their decision to purchase.
- A significant factor in determining whether substitution takes place is whether customers would incur costs in substituting products. High switching costs relative to the value of the product will make substitution less likely.
- Evidence on product characteristics may provide useful information where customer substitution patterns are likely to be influenced significantly by those characteristics. Where the objective characteristics of products are very similar and their intended uses the same this would be good evidence that the products are close substitutes. However, the following caveats should be noted. First, even where products apparently have very similar characteristics and intended use, switching costs and brand loyalty may affect how substitutable they are in practice. Second, just because products display similar physical characteristics, this does not necessarily mean that customers would view them to be close substitutes. For example, peak customers may not view rail travel during off peak times to be a close substitute for rail travel at peak times.[25] Third, products with

[24] Aberdeen Journals (No. 2), at [175] *et seq.*
[25] See Part 5 for a discussion of how time may affect market definition.

very different physical characteristics may be close substitutes if, from a customer's point of view, they have a very similar use.[26]

- Patterns in price changes can be informative. For example, two products showing the same pattern of price changes, for reasons not connected to costs or general price inflation, would be consistent with (although not proof of) these two products being close substitutes. Customer reactions to price changes in the past may also be relevant. Evidence that a relatively large proportion of customers had switched to a rival product in response to a relatively small price rise in the focal product would provide evidence that these two goods are close substitutes.[27] Equally price divergence over time, without significant levels of substitution, would be consistent with the two products being in separate markets.
- Evidence on own or cross price elasticities of demand may also be examined if it is available. The own price elasticity of demand measures the rate at which demand for a product (e.g. the focal product) changes when its price goes up or down. The cross price elasticity of demand measures the rate at which demand for a product (e.g. a rival product) changes when the price of another product (e.g. the focal product) goes up or down.
- In some cases 'critical loss' analysis may be relevant. One definition of critical loss is the minimum percentage loss in volume of sales required to make a 5 (or 10) per cent price increase on a product unprofitable. The critical percentage tends to be lower when an undertaking has a high mark up over unit costs (since each sale lost entails a relatively large loss in profit). However, the fact that an undertaking can set a high mark up might also demonstrate that its current customer base is not particularly price sensitive. These potentially opposing effects might need to be balanced and assessed in conjunction with other evidence (e.g. estimates of elasticities of demand).

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[26] See paragraph 3.5 for example.

[27] Although switching behaviour may be distorted if current prices are significantly different from competitive prices. See Part 5 for a discussion of market definition when prices are not competitive.

- Evidence on the price:concentration relationship may also be informative. Price:concentration studies examine how the price of a product in a distinct area varies according to the number (or share of supply) of other products sold in the same area. These studies are useful where data are available for several distinct areas with varying degrees of concentration. For example, if observations of prices in several geographic areas suggest that when two products are sold in the same area prices are significantly lower than when they are not, this might suggest that the two products are close substitutes (provided that it is possible to distinguish this from the effect of other factors which might explain the price differences).

Price discrimination

3.8 The test described in Part 2 assumes that the hypothetical monopolist charges all customers the same price for the focal product. However, in some cases the hypothetical monopolist may be able to charge some customers a higher price than others, where the price difference is not related to higher costs of serving those customers. This is called 'price discrimination'. Price discrimination requires that customers cannot arbitrage.[28] The undertaking could be able to discriminate between customers due to a variety of reasons, for example:

- some customers may face such high switching costs that they might be 'locked in' to purchasing a particular product (e.g. a customer might use a product as an input to its production process and switching to a rival product might entail costs of quality assuring that product as well as adjusting its production process)
- customer demand may differ according to time, e.g. demand for transport services at peak times is much less price sensitive than off peak demand for the same service, and
- customer demand for an input may differ according to the purpose for which it is used (for example, if different manufacturers transform the

[28] For example, customers purchasing at low prices must not be able to sell on sufficient quantities to customers paying higher prices to undermine price discrimination. Price discrimination by a dominant undertaking is considered in the competition law guideline *Assessment of conduct* (OFT414).

same input into different end products, they may have different derived demands for that input).[29]

3.9 Where a hypothetical monopolist would (or would be likely to) price discriminate significantly between groups of customers, each of these groups may form a separate market. If so, a relevant market might be defined as sales of the relevant product in the relevant geographic area to a particular customer group. For example, a hypothetical monopolist of a train service might be able to price discriminate between peak and off peak customers. In this case, peak travel and off peak travel might be in separate markets.[30]

Chains of substitution

3.10 Sometimes a focal product will be part of a long and unbroken chain of substitutes. For example, consider 5 products, labelled A to E, which are differentiated by their perceived quality.[31] Assume that the closer two products are in the alphabet, the more substitutable they are from the point of view of customers. Thus consumers whose favourite product is C consider B and D to be very good substitutes for C but consider A and E to be poorer substitutes for C. Even though all products in the chain are substitutes, this does not mean that the whole chain is the relevant market. For example, it may be that a hypothetical monopolist of three products next to each other in the chain could profitably sustain prices 5 to 10 per cent above competitive levels.[32] In short, the hypothetical monopolist test is a way of determining what range of products in the chain constitutes the relevant product market.

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[29] Derived demand describes the situation where the input purchaser's demand for the input is derived from the demand for the final product that the input is used to make.

[30] However, from a supply side perspective peak and off peak travel may be in the same market. Supply side substitution is discussed below.

[31] E.g. speed of spin cycle for washing machines, or sharpness of picture definition for digital cameras.

[32] It is worth noting that market definition may differ according to the focal product. In the example given, products A, B and C may form the relevant market when product B is the focal product, while products B, C and D may form the relevant market when product C is the focal product.

The supply side

3.11 This section addresses how the supply side of the market might be relevant to market definition.

3.12 If prices rise, undertakings that do not currently supply a product might be able to supply it at short notice and without incurring substantial sunk costs.[33] This may prevent a hypothetical monopolist profitably sustaining prices 5 to 10 per cent above competitive levels. This form of substitution is carried out by suppliers and hence is known as **supply side substitution.**

3.13 An example is the supply of paper for use in publishing.[34] Paper is produced in various different grades dependent on the coating used. From a customer's point of view, the different types of paper may not be viewed as substitutes, but because they are produced using the same plant and raw materials, it may be relatively easy for manufacturers to switch production between different grades. A hypothetical monopolist in one grade of paper might not profitably sustain supra competitive prices because manufacturers currently producing other grades would rapidly start supplying that grade.

3.14 Analysing supply side substitution raises similar issues to the analysis of barriers to entry (discussed further in the competition law guideline *Assessment of market power* (OFT415)). Supply side substitution can be thought of as a special case of entry – entry that occurs quickly (e.g. less than one year), effectively (e.g. on a scale large enough to affect prices), and without the need for substantial sunk investments. Supply side substitution addresses the questions of whether, to what extent, and how quickly, undertakings would start supplying a market in response to a hypothetical monopolist attempting to sustain supra competitive prices.

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[33] In this context, a sunk cost is a cost incurred on entering a market that is not recoverable on exiting that market. These could, for example, include investments in product placement, distribution, and production technology.

[34] The European Commission, in the course of a merger investigation, defined the market for the supply of paper for use in publishing based on supply side substitution in Torras/Sarrio Case IV/M166 OJ [1992] C58/00, [1992] 4 CMLR 341.

3.15 When assessing the scope for supply side substitution, the evidence from some or all of the following sources may be relevant:

- potential suppliers might be asked whether substitution was technically possible, about the costs of switching production between products, and the time it would take to switch production. The key question is whether it would be profitable to switch production given a small (e.g. 5 to 10 per cent) price increase above competitive levels
- potential suppliers might be asked whether they had spare capacity or were free or willing to switch production. Undertakings may be prevented from switching production because all their existing capacity was tied up, e.g. they may be committed to long term contracts. There might also be difficulties obtaining necessary inputs or finding distribution outlets. Undertakings may be unwilling to switch production from an existing product to a new one, if producing the former product is more profitable than the latter
- although potential suppliers may be able to supply the market, there may be reasons why customers would not use their products, so the views of customers might be sought, and
- more generally customers may also be able to supply wider information about potential suppliers. Customers that are businesses (not consumers) might take actions to encourage potential suppliers to enter.

3.16 There are two ways to account for supply side substitution when defining markets and calculating market shares. First, it might be appropriate to define a market based on the similarity of the conditions of supply. For example, adopting a market definition such as the 'supply of paper for use in publishing' might avoid the need to define and analyse many separate markets for individual grades of paper, for which the competitive assessment was qualitatively similar. If so, market shares would be based on overall capacity to provide paper for use in publishing.

3.17 Second, it might be appropriate to take each existing demand side market, assume prices in that market are sustained 5 to 10 per cent above competitive levels and consider what share of that market would likely be taken by new products produced by potential alternative

suppliers in response to that price rise. This share can then be attributed to potential alternative suppliers when calculating market shares.

3.18 The OFT will not factor supply side substitution into market definition unless it is reasonably likely to take place, and already has an impact by constraining the supplier of the product or group of products in question. What matters ultimately is that all competitive constraints from the supply side are properly taken into account in the analysis of market power. Whether a potential competitive constraint is labelled 'supply side substitution' (and so part of market definition) or 'potential entry' (and so not within the market) should not matter for the overall competitive assessment. If there is any serious doubt about whether or not to account for possible supply side substitution when defining the market and calculating market shares, the market will be defined only on the basis of demand side substitutability, and the supply side constraint in question will be considered when analysing potential entry.[35]

[35] Some competition authorities prefer to define markets solely on the demand side, leaving supply side issues to the analysis of new entry. Both approaches are valid and should produce the same conclusions on the question of market power, provided that supply side issues are examined at some point.

4 THE GEOGRAPHIC MARKET

4.1 Geographic markets are defined using the same process as that used to define product markets. The geographic market may be national (i.e. the United Kingdom), smaller than the United Kingdom (e.g. local or regional), wider than the United Kingdom (e.g. part of Europe including the United Kingdom), or even worldwide. This part outlines some practical issues which are particularly relevant to geographic market definition:

- demand side issues
- supply side issues, and
- imports

The demand side

4.2 As with the product market, the objective is to identify substitutes which are sufficiently close that they would prevent a hypothetical monopolist of the focal product in one area from profitably sustaining prices 5 to 10 per cent above competitive levels. The process starts by looking at a relatively narrow area – the **focal area**. This might be the area supplied by the parties to an agreement or the subject of a complaint about conduct or, if that area were relatively wide, past experience might suggest a narrower area that is more appropriate. The hypothetical monopolist test is applied to this area, and repeated over wider geographic areas as appropriate until the hypothetical monopolist would find it profitable to sustain prices 5 to 10 per cent above competitive levels in the area(s) in question (see Part 2 for further details of the hypothetical monopolist test).

4.3 The principles applied in defining the geographic market are the same as those for the product market. For example, the analysis of price discrimination and chains of substitution would proceed in the same way as set out in Part 3 above. The evidence used to define geographic markets on the demand side will usually be similar to the information used to define the product market (see paragraph 3.7). In addition to that evidence, the value of a product in relation to costs of search and transport is often an important factor in defining geographic markets. The higher the relative value, the more likely customers are to travel further in

search of cheaper supplies. The mobility of customers may also be a relevant factor.

4.4 For consumer products, geographic markets may often be quite narrow, e.g. where sufficient numbers of consumers are unlikely to switch to products sold in neighbouring towns or regions, let alone countries. For wholesaling or manufacturing markets, customers may be in a better position to switch between suppliers in different regions, providing transport costs are not too high.

The supply side

4.5 This entails looking at the potential for undertakings in other (e.g. neighbouring) territories to supply the focal area. When defining the geographic market, supply side substitution is analysed using the same conceptual approach set out for the product market. Therefore, the main evidence will usually mirror the information gathered on product market definition (see paragraph 3.15). Where the price of a product is low relative to its transport costs, this might indicate a relatively narrow geographic market.

Imports

4.6 When considering whether the geographic market should be defined more widely than a national market, data on imports may be informative. Significant imports of the product may indicate that the market is wider than a national market. However, the presence of imports in a territory will not always mean that the market is international, for a number of reasons. First, imports may come only from international operations of domestic suppliers, in which case they may not act as an independent constraint on domestic firms. Second, in order to import on a larger scale, international suppliers may require substantial investments in establishing distribution networks or branding their products in the destination country. Third, there may be quotas which limit the volume of imports into the destination country. These factors may mean that suppliers of the relevant product located outside the national market would not provide a sufficient constraint on domestic suppliers to be included in the same relevant geographic market.

4.7 Conversely, a lack of imports does not necessarily mean that the market cannot be international. The potential for imports may still be an important source of substitution should prices rise. For example, when the European Commission looked at a merger between bus manufacturers in Germany, it found that although imports were low at the time, there were no significant barriers to imports from the rest of the Community should prices in Germany rise.[36]

[36] Mercedes-Benz/Kassbohrer Case IV/M477 OJ [1995] L211/1, [1995] 4 CMLR 573.

5 OTHER ISSUES

Temporal markets

5.1 A third possible dimension to market definition is time. Examples of how the timing of production and purchasing can affect markets include:

- peak and off peak services. This can be a factor in transport services or utilities such as electricity supply
- seasonal variations, such as summer versus winter months, and
- innovation/inter-generational products. Customers may defer expenditure on present products because they believe innovation will soon produce better products or because they own an earlier version of the product, which they consider to be a close substitute for the current generation.

5.2 A time dimension might be appropriate where:

- it is not possible for customers to substitute between time periods. For example, peak customers might not view peak and off peak train tickets as substitutes, and
- suppliers cannot substitute between time periods. For example, capacity to produce fruit may vary between time periods and it may not be possible to store fruit from one period to another.

5.3 To some extent, the time dimension is simply an extension of the product dimension: i.e. the product can be defined as the supply of train services at a certain time of day.

The competitive price versus the current price

5.4 Throughout this guideline, the hypothetical monopolist test has been couched in terms of a hypothetical monopolist profitably sustaining prices above **competitive levels**. However, where an undertaking has market power, it may operate in a market where the current price is substantially different from the competitive price.

5.5 For example, an undertaking with market power may well have already raised prices above competitive levels to its profit maximising level. If so, the undertaking would not profitably sustain prices above **current** levels. If it tried to sustain higher prices, consumers would switch to purchasing

other products. However, it would be wrong to argue that these products prevented the undertaking from exercising market power and so it would usually be inappropriate to include them in the relevant market. This problem is sometimes known as the **cellophane fallacy** after a US case involving cellophane products.[37]

5.6 The possibility that market conditions are distorted by the presence of market power (or other factors) will be accounted for when all the evidence on market definition is weighed in the round. For example, where prices are likely to differ substantially from their competitive levels, caution must be exercised when dealing with the evidence on switching patterns as such evidence may not be a reliable guide to what would occur in normal competitive conditions.[38]

Previous cases

5.7 In many cases a market may have already been investigated and defined by the OFT or by another competition authority. Sometimes, earlier definitions can be informative when considering the appropriate product or area to use when commencing the hypothetical monopolist test. However, although previous cases can provide useful information, the market definition used may not always be the appropriate one for future cases. First, competitive conditions may change over time. In particular, innovation may make substitution between products easier, or more difficult, and therefore change the market definition. Therefore, the relevant market concerned must be identified according to the particular facts of the case in hand.[39]

5.8 Second, a previous product market definition that concerned an area outside the United Kingdom, would not necessarily apply to an area in the United Kingdom if the purchasing behaviour of customers differed significantly between those two areas.

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[37] US v El Du Pont de Nemours & Co [1956] 351 US 377.
[38] Evidence on market definition may be distorted if prices are sustained below competitive levels, as, for example, may occur in an investigation of predatory pricing. See Aberdeen Journals (No. 2) at [262].
[39] Aberdeen Journals Limited v Director General of Fair Trading [2002] CAT 4 at [139].

5.9 Third, behaviour by an undertaking with market power can affect market definition. For example, suppose an earlier investigation had defined a market to be relatively wide because of the scope for both demand side and supply side substitution. A dominant undertaking in that market might raise customer switching costs or foreclose some possibilities for supply side substitution. If so, this might affect the appropriate definition of the relevant market.

Differentiated products

5.10 When markets contain differentiated products (i.e. products that are differentiated by features such as brand, location or quality) there may not be a clear cut off point delineating the boundary of the market. This can mean that there is no clear distinction between products that are 'in' the market and those that lie outside it. Therefore, even if two products do not lie within the same market for the purposes of one investigation, this does not rule out the possibility that they will be in the same relevant market in another.[40]

Markets with portfolios of products

5.11 In some cases the relevant product market may consist of 'bundles' of what are otherwise distinct products. For example, if a relevant product market was 'one stop grocery shopping', the market may include bundles of groceries that normally make up a weekly shop. Whether this is appropriate depends on the investigation. For example, if the investigation concerned the supply of a particular grocery item to a retailer, it would usually be appropriate to consider that item as a distinct product as opposed to bundled together with other products. The perspective of customers will be important in assessing the appropriate frame of reference.

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[40] For example, recall the discussion of chains of substitution at paragraph 3.10 where products A to E were all substitutes for each other (to varying degrees) and where a hypothetical monopolist of three products next to each other in the chain could profitably sustain supra competitive prices. In this case, if the focal product is B alone, it is possible to define products A, B and C to be the relevant market. However, when investigating the conduct of an undertaking that supplies both products B and E, the appropriate frame of reference for the competitive assessment may include products A to E. (Of course, the analysis of competitive effects would account for the fact that customers do not view all products to be equally good substitutes.)

6 MARKET DEFINITION FOR AFTER MARKETS

6.1 An after market is a market for a **secondary product**, that is, a product which is purchased only as a result of buying a **primary product**. For example, a customer would purchase a printer cartridge (a secondary product) only for use with a printer (the primary product). Another example is replacement heads for razors (the secondary product) and razors (the primary product). The primary product and the secondary product are 'complementary'.[41]

6.2 Three possible ways of approaching market definition in after markets are often put forward:

- a 'system' market: a unified market for the primary product and the secondary product (e.g. a market for all razors **and** replacement heads)
- multiple markets: a market for primary products and separate markets for the secondary product(s) associated with each primary product (e.g. one market for all razors, individual markets for each type of replacement head), and
- dual markets: a market for the primary product and a separate market for the secondary product (e.g. one market for all razors, a separate market for all replacement heads).

6.3 The appropriate definition depends on the facts of the case. A system market is likely to be appropriate where customers engage in 'whole life costing' (see paragraphs 6.5 to 6.6 below), or where effective primary market competition ensures that the overall system price is not excessive, or where reputation effects mean that setting a supra competitive price for the secondary product would significantly harm a supplier's profits on future sales of its primary product.

6.4 Where none of the conditions set out in paragraph 6.3 apply, a multiple markets or a dual markets definition may be appropriate. The former is likely where, having purchased a primary product, customers are locked

[41] Products A and B are complementary products if the demand for product B goes up when the price of product A goes down by a relatively small amount, other things being equal.

in to using only a restricted number of secondary products that are compatible with the primary product. A dual markets definition is appropriate where secondary products are compatible with all primary products (and perceived to be so by customers).

Whole life costing

6.5 Whole life costing occurs where customers correctly anticipate the cost of future necessary purchases of the secondary market product when buying the primary product. For example, if a razor (with a 'life' of five replacement heads) costs £10, and each replacement head costs £2, the whole life cost of the razor would be £20. This depends on customers being able to form reasonable expectations on future prices of the secondary product when purchasing the primary product.

6.6 Whole life costing means that customers view the purchase of the primary and secondary product as a 'system', or a unified 'deal'. Whole life costing may mean that a 'system market' definition is appropriate where:

- it is relatively easy to obtain and comprehend information on the secondary market product, and relatively easy to predict how much of the secondary market product is likely to be required over the life time of the primary product, so that customers are **able** to whole life cost
- the price of (or likely expenditure on) the secondary product is a relatively high proportion of the primary product's price, so that customers are **likely** to whole life cost, and
- **sufficient** customers are able and likely to whole life cost so that it would be unprofitable for a supplier to set a supra competitive system price due to the number of customers that would adapt their purchasing behaviour in the primary market (within a reasonable period of time).[42]

Primary market competition

6.7 If suppliers produce both primary products and secondary products, and if, once the primary product is purchased, the same supplier's secondary

[42] This requires that enough, but not necessarily all, customers whole life cost and that it is not possible to price discriminate between those who do and those who do not.

product must also be purchased (as other suppliers' products would not be compatible), customers can be said to be 'locked in' once they have made their choice in the primary market. Therefore, customers might appear vulnerable to being charged supra competitive prices in the after market. In this sense, there is arguably a separate market for each secondary product.

6.8 However, the fact that customers may be locked in to particular after market purchases does not necessarily mean that, overall, a supplier can profitably sustain a system price above competitive levels. If there is effective competition in the primary market, undertakings would not earn excessive profits overall as any profits extracted in the after market would be 'competed away' in the primary market, resulting in lower priced primary products.[43] In this situation, a 'system' market definition is usually appropriate.

6.9 In short, where customers are locked in to purchasing a particular secondary product once they have purchased a primary product, competition problems are possible although they are more likely to arise where an undertaking has market power in the primary market.[44]

Reputation

6.10 A supplier might not wish to increase prices of its secondary product for existing customers if that would earn it a reputation for exploitation and significantly reduce its ability to attract new or repeat customers to its primary product. Reputation is more likely to be important where suppliers have the prospect of a relatively large numbers of new or repeat customers and where undertakings cannot price discriminate between new or repeat customers and other customers.

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[43] This would occur even if customers do not whole life cost.
[44] It should be noted that even if the overall system price is not excessive, the relative prices of the primary and secondary goods are not necessarily optimal.

ANNEXURE B

OFFICE OF FAIR TRADING

Powers of investigation

Draft competition law guideline for consultation

April 2004

OFT404a

Articles 81 and 82 of the EC Treaty and the Competition Act 1998 are applied and enforced in the United Kingdom by the Office of Fair Trading (the OFT). In relation to the regulated sectors these provisions are applied and enforced, concurrently with the OFT, by the regulators for communications matters, gas, electricity, water and sewerage, railway and air traffic services (under section 54 and schedule 10 of the Competition Act 1998) (the Regulators). Throughout the guidelines, references to the OFT should be taken to include the Regulators in relation to their respective industries, unless otherwise specified.

The following are Regulators:

- the Office of Communications (OFCOM)
- the Gas and Electricity Markets Authority (OFGEM)
- the Northern Ireland Authority for Energy Regulation (OFREG NI)
- the Director General of Water Services (OFWAT)
- the Rail Regulator[1] (ORR), and
- the Civil Aviation Authority (CAA).

This guideline provides general advice and information about the application and enforcement by the OFT of Articles 81 and 82 of the EC Treaty and the Chapter I and Chapter II prohibitions contained in the Competition Act 1998. It is intended to explain these provisions to those who are likely to be affected by them and to indicate how the OFT expects them to operate. Further information on how the OFT has applied and enforced competition law in particular cases may be found in the OFT's decisions, as available on its website from time to time.

This guideline is not a substitute for the EC Treaty nor for regulations made and notices provided under it. Neither is this guideline a substitute for the Competition Act 1998 and the regulations and orders made under it. It should be read in conjunction with these legal instruments, Community case law and United Kingdom case law. Anyone in doubt about how they may be affected by the EC Treaty and the Competition Act 1998 should seek legal advice.

[1] This will change to the Office of Rail Regulation on 5 July 2004.

CONTENTS

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1 INTRODUCTION

1.1 The Competition Act 1998 (the Act) provides the Office of Fair Trading (the OFT) with various powers to investigate suspected anti-competitive behaviour. This guideline describes these powers of investigation.

1.2 First, Part I of the Act provides the OFT with powers to investigate on its own behalf suspected infringements of both Article 81 and Article 82 of the EC Treaty[2] ('Article 81' and 'Article 82' respectively) and the Chapter I and Chapter II prohibitions contained within Part I of the Act ('the Chapter I prohibition' and 'the Chapter II prohibition' respectively). These powers enable the OFT to:

- require the production of specified documents or specified information[3]
- enter business premises without a warrant[4], and
- enter and search business and/or domestic premises with a warrant.[5]

1.3 Parts 3 to 5 of this guideline describe when each of these powers can be used, the extent of each power and the procedures that must be followed. The limitations on the use of these powers are described in Part 6 and the offences committed by a person who fails to comply when these powers are exercised are described in Part 7. The OFT's power to require information when determining whether to withdraw the benefit of an exclusion is described in Part 8.

1.4 Second, Part 2 of the Act provides the OFT with powers to assist, or act on behalf of, the European Commission in connection with European Commission investigations relating to Article 81 and Article 82. The scope of these powers is described in Part 9.

1.5 Third, Part 2A of the Act provides that the OFT can carry out an inspection in the United Kingdom, at the request of a national competition authority of another Member State (an NCA) on behalf of that NCA, for the purpose of assisting it in deciding whether there has been an infringement of Article 81 or Article 82. When the OFT conducts

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[2] The Treaty of Rome, establishing the European Community, as consolidated by the Treaty of Amsterdam.
[3] Section 26.
[4] Section 27.
[5] Sections 28 and 28A.

such investigations it will use similar powers to those it has available to investigate suspected infringements of Article 81 and Article 82 on its own behalf. The OFT's role in such investigations is described in Part 10.

1.6 The Regulators have concurrent powers to investigate suspected infringements of Article 81 and Article 82 and the Chapter I prohibition and Chapter II prohibition under Part I of the Act. The Regulators do not have investigative powers under Part 2 or Part 2A of the Act and therefore do not have any powers to investigate suspected infringements of Article 81 or Article 82 in connection with an investigation by the European Commission or on behalf of NCAs of other Member States. However, where appropriate, Regulators may participate in investigations conducted by the OFT under Part 2 or Part 2A of the Act.

2 TRIGGER FOR THE USE OF THE POWERS OF INVESTIGATION

2.1 Section 25 of the Act provides that the OFT, when acting on its own behalf, may carry out an investigation if there are reasonable grounds for suspecting:

- that an agreement[6] falls within Article 81 and/or the Chapter I prohibition, and/or
- that there has been an infringement of Article 82 and/or the Chapter II prohibition.

The formal powers of investigation can only be used where this requirement is met. Thus the OFT is not obliged to determine whether the conditions in Article 81(3) of the EC Treaty (in the case of an agreement which is suspected to fall within Article 81) or section 9(1) of the Act (in the case of an agreement which is suspected to fall within the Chapter I prohibition) may be satisfied before it may conduct an investigation.[7]

2.2 Whether there are reasonable grounds for suspicion will depend upon the OFT's assessment of the information available. Examples of information that may be sources of reasonable grounds for suspicion include information provided by disaffected members of a cartel, statements from employees or ex-employees, or a complaint.

2.3 However, in the case of an agreement which is suspected to fall within the Chapter I prohibition, if the OFT considers that the agreement has the benefit of a parallel exemption or a domestic block exemption, then it cannot investigate unless it has reasonable grounds for suspecting that the circumstances are such that it could exercise its power to cancel the exemption. Similarly, in the case of an agreement which is suspected to fall within Article 81, if the OFT considers that the agreement has the benefit of a Commission block exemption regulation, then it cannot investigate unless it has reasonable grounds for suspecting that the

[6] References in this guideline to 'agreements' should, unless otherwise stated or the context demands it, be taken to include decisions by associations of undertakings and concerted practices.

[7] Further details of the conditions in Article 81(3) of the EC Treaty and section 9(1) of the Act are set out in the competition law guideline *Article 81 and the Chapter I prohibition* (OFT401).

conditions for the withdrawal of the benefit of the regulation in question may be satisfied.[8]

2.4 Parts 4 to 6 below describe the OFT's formal powers of investigation. It should be noted that the OFT may also obtain information about undertakings[9], agreements, practices and markets through informal enquiries. Such enquiries, which may be made at a meeting, in written correspondence or in a telephone conversation, may be made in addition to, or instead of, using the formal powers of investigation set out in the Act. The OFT cannot compel an undertaking to respond to an informal enquiry which is not backed by statutory powers. Undertakings are encouraged to cooperate.

[8] For a discussion of EC and domestic block exemptions and parallel exemptions under the Act and the circumstances in which they may be cancelled or withdrawn (as the case may be), see the competition law guideline *Article 81 and the Chapter I prohibition* (OFT401).

[9] The term undertaking is not defined in the EC Treaty or the Act, but its meaning has been set out in Community law. It covers any natural or legal person engaged in economic activity, regardless of its legal status and the way in which it is financed. It includes companies, partnerships, firms, businesses, individuals operating as sole traders, agricultural cooperatives, associations of undertakings (e.g. trade associations), non-profit making organisations and (in some circumstances) public entities that offer goods or services on a given market.

3 PRODUCTION OF SPECIFIED DOCUMENTS AND INFORMATION

When the power can be used

3.1 Where the OFT has reasonable grounds for suspecting that an agreement falls within one or both of Article 81 and the Chapter I prohibition, and/or that one or both of Article 82 and the Chapter II prohibition have been infringed, it may, under section 26 of the Act, require a person to produce specified documents or to provide specified information. This is the power of investigation that the OFT uses most frequently. The section 26 power is exercised by written notice, the contents of which are described in paragraph 3.8 below.

3.2 It is not necessary for the section 26 power to be used before carrying out an inspection (described in Parts 5 and 6 below). For example, it may be used for the first time either during or after an inspection to clarify facts that have emerged.

3.3 A person may receive a notice requiring the production of documents or information on more than one occasion during the course of an investigation. For example, the OFT may require a person to produce further information after considering the material produced in response to an earlier notice under section 26.

The scope of the power

3.4 The OFT can require any person to produce documents or information that it considers relate to any matter relevant to the investigation. The OFT is not limited to approaching the undertakings suspected of infringement. For example, the notice may be addressed to third parties such as complainants, suppliers, customers and competitors.

3.5 The OFT can also:

- take copies or extracts from any document produced
- require the person required to produce the document (or any past or present officer or employee of that person) to provide an explanation of the document if it is produced
- require the person required to produce the document to state, to the best of their knowledge or belief, where the document can be found, if the document is not produced.

3.6 The term 'document' includes 'information recorded in any form'[10]. This definition includes records, such as invoices or sales figures, held on computer. 'Specified' means documents or information that are specified or described in a written notice or that fall within a category which is so specified or described. A category of documents may include, for example, invoices, agreements and minutes of meetings.

3.7 The OFT can use the power to require the production of specified information to require the compilation and production of information that is not already in recorded form. For example, a person may be asked to provide market share information or to provide a description of a particular market using their knowledge and experience or the knowledge and experience of their staff.

The procedure

3.8 The power to require the production of documents or information using section 26 of the Act is exercised by serving a written notice. The written notice will usually be sent by post or by fax. The written notice must:

- state the subject matter and purpose of the investigation
- specify or describe the documents or information, or categories of documents or information, required, and
- set out the nature of the offences created by the Act, including the offences that may be committed when the addressee of the notice: fails to comply with a requirement under the notice; destroys, disposes of, falsifies or conceals a document; or provides false or misleading information.

3.9 The notice may also state the time and place at which a document or information must be produced and the manner and form in which it is to be produced. For example, a person may be required to produce the documents or information at a specified address on a designated date at a particular time. If a document is produced, the OFT may require that an explanation of the document is provided. A person required by the OFT to provide an explanation of a document may be accompanied by a legal adviser.

[10] Section 59.

3.10 In specifying documents or information in a written notice, the OFT will not seek more documents or information than it believes are necessary for the investigation as at the date of the notice.

3.11 When setting the appropriate time limit for the production of documents or information, the OFT will consider the amount and the complexity of the information required, the resources available to the individual or undertaking and the urgency of the case.

3.12 The notice may be addressed to individuals or undertakings. Where a notice is addressed to an undertaking, the appropriate person to respond is the person who is authorised by the undertaking to respond on behalf of the undertaking. Where a notice is addressed to an individual, that individual must respond and it is not acceptable for another person to respond on their behalf. This does not prevent an individual from obtaining legal representation in relation to a notice.

4 POWER TO ENTER BUSINESS PREMISES WITHOUT A WARRANT

4.1 If the OFT has reasonable grounds for suspecting that an agreement falls within one or both of Article 81 and the Chapter I prohibition, and/or that one or both of Article 82 and the Chapter II prohibition have been infringed, it may conduct an investigation and has the power to enter premises to carry out inspections, either with or without a warrant. These powers enable the OFT to enter premises and require the production of documents relevant to an investigation.

4.2 The power to carry out inspections without a warrant is described in this Part of the guideline. This power is limited to business premises, which are defined in the Act as meaning any premises (or part of premises) not used as a dwelling[11]. The power to carry out inspections of both business and domestic premises when a warrant has been obtained is described in Part 5.

When the power can be used

4.3 Any officer of the OFT who is authorised in writing by the OFT to enter premises (an authorised officer) may enter business premises in connection with an investigation if they have given the occupier of the premises at least two working days' written notice of the intended entry. The occupier of the premises need not be suspected of an infringement. For example, the premises of a supplier or customer may be entered using this power.

4.4 An authorised officer may enter business premises in connection with an investigation without a warrant and without notice if:

- the OFT has a reasonable suspicion that the premises are, or have been, occupied by a party to an agreement which it is investigating or an undertaking whose conduct it is investigating, or
- the authorised officer has been unable to give notice to the occupier, despite taking all reasonably practicable steps to give notice.

[11] Section 27(6).

The scope of the power

4.5 An authorised officer entering business premises without a warrant may require:

- any person on the premises to produce any document that the authorised officer considers relates to any matter relevant to the investigation. For example, an employee may be asked to produce minutes of any meetings with competitors, the diaries of specified directors, sales data or invoices. The authorised officer can take copies of, or extracts from, any document produced
- any person on the premises to provide an explanation of any document produced. For example, an employee may be requested to provide an explanation of the entries or codes on an invoice or spreadsheet
- any person to state, to the best of their knowledge and belief, where any document that the authorised officer considers relates to any matter relevant to the investigation can be found
- any information which is stored in any electronic form and is accessible from the premises to be produced in a form in which it can be read and can be taken away, and
- take any other steps necessary in order to preserve the documents or prevent interference with them. This includes requiring that the premises (or any part of the premises, including offices, files and cupboards) be sealed for such time as is reasonably necessary to enable the inspection to be completed. This time period will not be for longer than 72 hours, except where an undertaking consents to a longer time or where access to documents is unduly delayed, such as by the unavailability of a person who can provide access.

4.6 An authorised officer may take with him any equipment that he deems necessary when entering any premises under this power. For example, the authorised officer may take portable computer equipment and tape recording equipment.

The procedure

4.7 If the authorised officer is carrying out an inspection of business premises without a warrant after giving at least two working days' written notice, the written notice must state:

- the subject matter and purpose of the investigation, and

- the nature of the offences that may be committed if a person fails to comply when the powers of investigation are exercised (described in Part 7 below).

4.8 If the authorised officer is entering the premises without a warrant and without written notice, he may enter only on production of evidence of his authorisation by the OFT and a document indicating:

- the subject matter and purpose of the investigation, and
- the nature of the offences that may be committed if a person fails to comply when the powers of investigation are exercised (described in Part 7 below).

4.9 The authorised officer will normally arrive at the premises during office hours. On entering the premises, the authorised officer will produce evidence of his identity. He will also hand over a separate document which sets out the powers of the authorised officer and states that the occupier may request that a legal adviser is present. Where possible, the person in charge at the premises should designate an appropriate person to be a point of contact for the authorised officer during the inspection.

Access to legal advice

4.10 An undertaking being investigated will be able to contact its legal advisers during the course of an inspection. The authorised officer will grant a request to wait a short time for legal advisers to arrive at the premises before the inspection continues, if he considers that it is reasonable to do so in the circumstances. The practice of the OFT will go no further than the practice of the European Commission when determining how long to wait for legal advisers to arrive.

4.11 The exercise of the right to consult a legal adviser must not unduly delay or impede the inspection. Any delay must be kept to a strict minimum. The main concern is that any delay might provide an opportunity for evidence to be tampered with or for other parties to a suspected infringement to be warned about the inspection, for example, by telephone or e-mail. To reduce this concern the authorised officer may attach such conditions as he considers appropriate when agreeing a reasonable time to wait. The conditions could include, for example, the sealing of cabinets, keeping business records in the same state and place as when the authorised officer arrived, suspending external e-mail and allowing the authorised officer to enter and remain in occupation of

selected offices. If an undertaking has an in-house legal adviser on the premises, or if the undertaking has been given notice of the inspection, the authorised officer will not wait for an external legal adviser to arrive.

5 POWER TO ENTER AND SEARCH ANY PREMISES WITH A WARRANT

5.1 An application can be made to a judge of the High Court (or the Court of Session in Scotland) for a warrant for a named officer of the OFT (named officer) and other authorised officers[12] to enter and search both business and domestic premises.

When the power can be used

5.2 In relation to business premises, the Act identifies three circumstances in which a judge of the High Court or Court of Session may issue a warrant to authorise a named officer and any other authorised officers to enter and search business premises specified in the warrant. The judge must be satisfied that there are reasonable grounds for suspecting that there are documents on the premises to be searched:

- which the OFT has required to be produced, either by written notice (section 26 of the Act) or in the course of an inspection without a warrant (section 27 of the Act), and which have not been produced
- which the OFT has the power to require to be produced by written notice (section 26 of the Act), but which, if required to be produced, would be concealed, removed, tampered with or destroyed, or
- which an authorised officer could have required to be produced in an inspection without a warrant (section 27 of the Act). In these circumstances the judge must also be satisfied that an authorised officer has attempted but has been unable to enter the premises without a warrant.

5.3 The second ground for obtaining a warrant identified above (that documents would be concealed or removed etc. if required to be produced) is the only means by which the OFT is able to carry out an inspection of business premises with a warrant without using one of the other investigatory powers first.

5.4 Domestic premises are defined in the Act as premises (or any part of premises) used as a dwelling and also used in connection with the affairs of an undertaking or association of undertakings or where documents

[12] A named officer is also an authorised officer.

relating to the affairs of an undertaking or association of undertakings are kept.[13] In relation to domestic premises, the Act identifies two circumstances in which a judge of the High Court or Court of Session may issue a warrant to authorise a named officer and any other authorised officers to enter and search domestic premises specified in the warrant. The judge must be satisfied that there are reasonable grounds for suspecting that on any domestic premises to be searched there are documents:

- which the OFT has required to be produced by written notice (section 26 of the Act) and which have not been produced, or
- which the OFT has the power to require to be produced by written notice under section 26 of the Act; and if the documents were required to be produced, they would not be produced and would be concealed, removed, tampered with or destroyed.

The scope of the power

5.5 The warrant will authorise a named officer, and any other authorised officers to:

- Enter the premises specified in the warrant using such force as reasonably necessary. Authorised officers entering the premises will be entitled to use force only if they are prevented from entering the premises and may use only such force as is reasonably necessary for the purpose of gaining entry. Authorised officers cannot use force against any person.
- Search the premises and take copies of, or extracts from, any documents appearing to be of the kind in respect of which the warrant was granted (identified in paragraph 5.8 below). Authorised officers can search offices, desks and filing cabinets etc. to find such documents.
- Take possession of any documents appearing to be of the kind in respect of which the warrant was granted if such action appears to be necessary for preserving the documents or preventing interference with them, or if it is not reasonably practicable to take copies of the documents on the premises. In most cases the authorised officers will

[13] Section 28A(9).

take copies of documents. Original documents that are taken will be returned within three months.

- Take any other steps which appear necessary in order to preserve the documents or prevent interference with them. This includes requiring that the premises (or any part of the premises, including offices, files and cupboards) be sealed for such time as is reasonably necessary to enable the inspection to be completed. This time period will not be for longer than 72 hours, except where an undertaking consents to a longer time or where access to documents is unduly delayed, such as by the unavailability of a person who can provide access.
- Require any person to provide an explanation of any document appearing to be of the kind in respect of which the warrant was granted or to state to the best of their knowledge and belief where such document may be found.
- Require any information which is stored in any electronic form and is accessible from the premises to be produced in a form in which it can be read and can be taken away.
- Take and remove copies of any document or information in order to determine later whether (or the extent to which) the document or information is of a kind in respect of which the warrant was granted, where it is not reasonably practicable to determine this on the premises.[14]
- Take and remove copies of any document or information where it is not reasonably practicable to separate a document or information which is of a kind in respect of which the warrant was granted from a document or information which is not.[15]

5.6 Authorised officers entering premises under a warrant may take with them such equipment as they deem necessary. This will include equipment that can be used to enter the premises using reasonable force (for example, equipment that can be used to break locks) as well as equipment that can be used to facilitate the search (for example, computer equipment).

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[14] Section 50(1) Criminal Justice and Police Act 2001.
[15] Section 50(2) Criminal Justice and Police Act 2001.

5.7 The warrant may also authorise other persons to accompany the authorised officers on an inspection, such as computer technicians or industry experts.

5.8 The category of documents that authorised officers can take copies of etc. (as set out in paragraph 5.5 above) depends on the ground under which the warrant was obtained:

- Where the warrant was granted because a person failed to produce documents, the authorised officers can take copies etc. of any documents which were required to be produced and were not produced under section 26 or 27 of the Act.
- Where the warrant was granted because there were reasonable grounds for suspecting that the documents would have been tampered with etc., the authorised officers can take copies etc. of any documents which they had the power to require to be produced under section 26 of the Act. In addition, if the judge is satisfied that it is reasonable to suspect that there are also other documents relating to the investigation on the premises, the warrant will also authorise the authorised officers to take copies etc. of any such document.
- Where the warrant was granted because an authorised officer was unable to enter premises, the authorised officers can take copies etc. of any document which could have been required to be produced under section 27 of the Act had they been able to enter the premises.

The procedure

5.9 The powers set out in paragraphs 5.5 to 5.8 may only be exercised on production of the warrant.

5.10 The warrant must indicate:

- the subject matter and purpose of the investigation, and
- the nature of the offences committed if a person fails to comply when the powers of investigation are exercised.

The warrant continues in force for one month from the date of issue.

5.11 The authorised officers will normally arrive at the premises during office hours. On entering the premises, the named officer will produce evidence of their identity. The named officer will also hand over a document which sets out the powers of the authorised officers and states that the occupier may request that a legal adviser be present. Where possible, the

person in charge at the premises should designate an appropriate person to be a point of contact for the authorised officers during the inspection.

5.12 If there is no one at the premises, the named officer must take reasonable steps to inform the occupier of the premises of the intended entry. If the occupier is informed, the occupier or their legal or other representative must be given a reasonable opportunity to be present when the warrant is executed. If the named officer has been unable to inform the occupier of the intended entry, he is under a duty to leave a copy of the warrant in a prominent place on the premises. On leaving premises that are unoccupied the named officer must leave them secured as effectively as he found them.

Access to legal advice

5.13 See paragraphs 4.10 to 4.11 above.

6 LIMITATIONS ON THE USE OF THE POWERS OF INVESTIGATION UNDER PART I OF THE ACT

Privileged communications

6.1 The power to require the production of documents under Part I of the Act, either on written notice or during an inspection, does not extend to privileged communications[16]. A person can refuse to produce or disclose a document that is a privileged communication. A privileged communication is defined by section 30 of the Act to mean a communication:

- between a professional legal adviser and his or her client, or
- made in connection with, or in contemplation of, legal proceedings and for the purposes of those proceedings

which would be protected from disclosure in proceedings in the High Court on grounds of legal professional privilege or in the Court of Session on grounds of confidentiality of communications.

6.2 When the OFT is investigating suspected infringements of Article 81 or Article 82 in the UK on its own initiative, or at the request of another NCA or on behalf of the European Commission, UK rules on legal professional privilege ('privilege') will apply. This means that the communications of in-house lawyers, in addition to lawyers in private practice, can benefit from privilege. This is a different rule to that applied by the European Commission, which does not allow the communications of in-house lawyers to benefit from privilege.[17]

6.3 Whilst UK privilege rules would apply to cases being investigated in the UK by the OFT on its own behalf under national and EC law, the OFT could be sent the communications of in-house lawyers by an NCA from another Member State where the communication of in-house lawyers are not privileged. Under those circumstances, the OFT may use the documentation received from the other NCA in its investigation.

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[16] Section 30.
[17] Case 155/79 AM & S Europe v Commission [1982] ECR 1575, [1982] CMLR 264.

6.4 The European Commission's privilege rules (which do not extend to in-house counsel) will continue to apply to investigations that it conducts on its own behalf.

Self-incrimination

6.5 Privilege against self-incrimination is an aspect of the right to a fair trial guaranteed by Article 6 of the European Convention on Human Rights[18]. An equivalent privilege against self-incrimination has also been recognised in EC jurisprudence in relation to investigation of suspected breaches of Article 81 and Article 82[19].

6.6 The OFT may compel an undertaking to provide specified documents or specified information but cannot compel the provision of answers which might involve an admission on its part of the existence of a competition law infringement, which it is incumbent upon the OFT to prove. The OFT may, however, request documents or information relating to facts, for example, whether a particular employee attended a particular meeting.

6.7 A statement made by a person in response to a requirement imposed by the OFT when investigating suspected competition law infringements may not generally be used in evidence against that person on a prosecution for the cartel offence under the Enterprise Act 2002 (the Enterprise Act)[20].

Disclosure of confidential information

6.8 Part 9 of the Enterprise Act imposes limits on the disclosure of information relating to the affairs of any individual or to any particular business of an undertaking, that is obtained in connection with the exercise of any function of the OFT under the Act (including the OFT's powers of investigation under the Act).

6.9 The Enterprise Act requires that such information is not to be disclosed during the lifetime of the individual in question or while the undertaking continues in existence unless disclosure is specifically

[18] This is given effect in the United Kingdom by the Human Rights Act 1998.
[19] See paragraphs 77-78 of the judgment in Case T-112/98 Mannesmannröhren-Werke AG v Commission [2001] ECR II-729.
[20] Section 30A.

permitted under Part 9 or is made pursuant to a power or duty to disclose information which exists apart from Part 9.

6.10 Part 9 of the Enterprise Act provides a number of categories of permitted disclosure[21]. For example, the OFT is permitted to disclose information for the purpose of facilitating any of its functions (including its functions under the Act and the Enterprise Act)[22]. Disclosure is also permitted with the consent either of the individual to whose affairs the information relates or, where the information relates to the business of an undertaking, the consent of the person carrying on the business. In either case, if the information was obtained by the OFT from a different person (who had the information lawfully and whose identity is known to the OFT) then the consent of that person will also be required[23].

6.11 Before making disclosure (for example, where such information is included in material to be published), the OFT must have regard to three considerations:

- the need to exclude, so far as is practicable, information the disclosure of which would in its opinion be contrary to the public interest[24]
- the need to exclude, so far as is practicable, commercial information disclosure of which it thinks might significantly harm the legitimate business interests of the undertaking to which it relates, or information relating to the private affairs of an individual disclosure of which it thinks might significantly harm the individual's interests[25], and
- the extent to which the disclosure of such information is necessary for the purposes for which it is to be disclosed[26].

The OFT may have to edit documents it proposes to disclose to remove information: for example, by blanking out parts of documents or by aggregating figures.

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[21] Sections 239 to 243 Enterprise Act.
[22] Section 241(1) Enterprise Act.
[23] Section 239 Enterprise Act.
[24] Section 244(2) Enterprise Act.
[25] Section 244(3) Enterprise Act.
[26] Section 244(4) Enterprise Act.

6.12 Where, under the *OFT's Rules*, the OFT proposes to disclose any information identified by the person supplying it as being confidential, the OFT will inform the person supplying the information of its proposed action, and give that person a reasonable opportunity to make representations to the OFT, if it is reasonably practicable to do so[27].

6.13 For disclosure of information to the Commission and NCAs, the OFT has a power to disclose apart from Part 9, provided by the Modernisation Regulation[28]. This allows disclosure to the Commission and NCAs for the purpose of applying Articles 81 and 82. Part 9 of the Enterprise Act also specifically permits disclosure of information where disclosure is required for the purpose of a Community obligation[29]. Where information relates to the affairs of any individual or to any business of an undertaking, the OFT will have regard to the three considerations outlined at paragraph 6.11 above before making disclosure to the Commission or an NCA. However, such disclosure is not made under the *OFT's Rules* and, accordingly, the procedure outlined in paragraph 6.12 above does not apply.

[27] The Competition Act 1998 (Office of Fair Trading's Rules) Order 2004 (SI 2004/[ ]), Rule 6(1).
[28] Article 12.
[29] Section 240 Enterprise Act.

7 OFFENCES RELATING TO THE POWERS OF INVESTIGATION UNDER PART I OF THE ACT

7.1 The Act sets out a number of criminal offences which may be committed where a person fails to co-operate when the powers of investigation set out in Part I of the Act are exercised. It is an offence for a person to:

- fail to comply with a requirement imposed under the powers of investigation in the Act (subject to certain defences, see below)
- intentionally obstruct an authorised officer carrying out an inspection either with or without a warrant
- intentionally or recklessly destroy or otherwise dispose of or falsify or conceal a document that they have been required to produce or cause or permit its destruction, disposal, falsification or concealment, or
- provide information that is false or misleading in a material particular if they know, or are reckless as to whether, it is false or misleading, either to the OFT or to another person such as an employee or legal adviser, knowing that it will be used for the purpose of providing information to the OFT.

7.2 A person who fails to comply with a requirement to produce a document has a defence if they can prove that the document was not in their possession or control and that it was not reasonably practicable to comply with this requirement. It is a defence for a person who fails to comply with a requirement to provide information or an explanation of a document or to state where a document is to be found if they can prove that they had a reasonable excuse for failing to comply with the requirement.

7.3 Failing to comply with a requirement imposed under section 26 or section 27 of the Act is not an offence if the OFT has failed to act in accordance with the provision in question.

7.4 The officer as well as the body corporate is guilty of any of the offences described above if the offence that is committed by a body corporate is proved to have been committed with the consent or connivance of an officer or to be attributable to their neglect. An 'officer' is defined to mean a director, manager, secretary or other similar officer of the company or a person purporting to act in any such capacity. Where the affairs of the body corporate are managed by its members, a member is also guilty of an offence if the offence of the body corporate is proved to

have been committed with the consent or connivance of the member or to be attributable to their neglect as if they were a director. In Scotland, a partner or person purporting to be a partner, as well as the partnership, may be guilty of the offence.

7.5 Offences will be tried either summarily in the Magistrates' Court or Sheriff Court or, in the case of more serious offences, on indictment in the Crown Court or the High Court of the Justiciary. The Code for Crown Prosecutors will be followed in determining the appropriate court in which to commence proceedings.

7.6 A person convicted of intentionally obstructing an authorised officer carrying out an inspection without a warrant will be liable to a fine. The consequences of intentionally obstructing an authorised officer exercising their powers under a warrant are more serious. Conviction on indictment may lead to a fine, to imprisonment for up to two years, or both.

7.7 The sanctions that may be imposed by the courts on a person found guilty of each offence described in paragraph 7.1 are set out in the table overleaf. The sanctions that are available for each offence differ according to whether the person is found guilty on summary conviction or on indictment.

Offence	Sanction on summary conviction	Sanction on conviction on indictment
Fail to comply with a requirement imposed under the powers of investigation	Fine of up to the statutory maximum (currently £5000)	Unlimited fine
Intentionally obstruct an authorised officer carrying out an inspection without a warrant	Fine of up to the statutory maximum	Unlimited fine
Intentionally obstruct an authorised officer carrying out an inspection with a warrant	Fine of up to the statutory maximum	Unlimited fine and/or up to two years' imprisonment
Intentionally or recklessly destroy, dispose of, falsify or conceal a document the production of which has been required or cause or permit its destruction etc.	Fine of up to the statutory maximum	Unlimited fine and/or up to two years' imprisonment
Knowingly or recklessly provide information that is false or misleading in a material particular	Fine of up to the statutory maximum	Unlimited fine and/or up to two years' imprisonment

8 POWERS OF INVESTIGATION IN RELATION TO EXCLUSIONS

8.1 The Act specifically excludes certain categories of agreements and/or conduct from the Chapter I prohibition or the Chapter II prohibition[30] (see competition law guideline *The major provisions* (OFT400)). These do not provide any exclusion from Article 81 or Article 82. In relation to some of these categories, the OFT is able to withdraw the application of the exclusion from a particular agreement in certain circumstances. Those categories are:

- certain agreements falling within the mergers exclusion[31]
- agreements which are the subject of a direction under section 21(2) of the Restrictive Trade Practices Act 1976[32]
- agreements which relate to production of or trade in 'agricultural products' as defined in the EC Treaty and in Council Regulation (EEC) No 26/62, or to certain farmers' cooperatives[33], and
- certain vertical agreements and land agreements which fall within the relevant order made pursuant to section 50 of the Act[34].

8.2 The OFT may issue a direction to withdraw the application of an exclusion from a particular agreement falling within one of the above categories if it considers that the agreement would fall within the Chapter I prohibition and that it would be unlikely to satisfy the conditions in section 9(1) of the Act.

8.3 If the OFT is considering withdrawing an exclusion, it may require any party to the agreement in question to give it such information in connection with the agreement as it requires. This must be done by sending a written notice. If the party in question fails to provide the information required within the time period specified in the *OFT's Rules*[35]

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[30] Section 3 and schedules 1-4.
[31] Schedule 1.
[32] Schedule 3. However, the exclusion is repealed with effect from 1 May 2007: see the competition law guideline *The major provisions* (OFT400).
[33] Schedule 3.
[34] The exclusion for vertical agreements is repealed with effect from 1 May 2005: see the competition law guideline *Vertical agreements* (OFT419). See the competition law guideline *Land agreements* (OFT420) for further detail in relation to land agreements.
[35] Rule 14(3).

without reasonable excuse, the OFT may give a direction withdrawing the exclusion.

8.4 Section 194A of the Broadcasting Act 1990 allows the OFT and OFCOM (but not the other Regulators) to exercise the powers of investigation in the Act in respect of certain agreements relating to television news provision. A special procedure must, however, be observed before the powers can be exercised.

8.5 Section 160 of the Financial Services and Markets Act 2000 allows the OFT (but not the Regulators) to exercise powers to request information in respect of its competition scrutiny of the regulating provisions and practices of the Financial Services Authority. Section 305 of the Financial Services and Markets Act 2000 allows the OFT (but not the Regulators) to exercise powers to request information in respect of its competition scrutiny of recognised investment exchanges and clearing houses.

9 POWER TO ASSIST THE EUROPEAN COMMISSION IN ITS INVESTIGATIONS

9.1 The European Commission has formal powers enabling it to undertake investigations relating to Article 81 and Article 82. Part 2 of the Act and EC Regulation 1/2003 (the Modernisation Regulation)[36] together provide the OFT with powers to assist the European Commission. The OFT may actively participate in European Commission investigations relating to Article 81 or Article 82 in three ways:

- the OFT may be required to **assist** the European Commission when European Commission officials carry out an inspection of business premises in the United Kingdom
- the European Commission may request that the OFT carry out an inspection of business premises **on its behalf**, and/or
- the OFT may be required to **assist** the European Commission when European Commission officials carry out an inspection of non-business premises in the United Kingdom.

9.2 These powers are similar to the power to enter and search premises with a warrant described in Part 5. These powers are not available to the Regulators; however, they may participate in inspections carried out by the OFT on behalf of the European Commission if the industry being investigated falls within their area of expertise.

9.3 When **assisting** the European Commission with an inspection of business premises, the officers of the OFT have the same powers as an official authorised by the European Commission[37]. The OFT may obtain a warrant where a European Commission inspection is being, or is likely to be, obstructed. The warrant will authorise officers of the OFT and European Commission officials to enter the premises in question and to search for books and records that the officials have the power to examine, using such force as is reasonably necessary for the purpose.

9.4 When the OFT is carrying out an inspection of business premises **on behalf of** the European Commission, the officers of the OFT will have

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[36] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (OJ L1, 4.1.03, p1). See the competition law guideline *Modernisation* (OFT442) for further details.
[37] Article 20(5) of the Modernisation Regulation.

been given an authorisation under the Act which has the effect of providing them with the powers of an official authorised by the European Commission[38]. This means that the officers will possess further powers that are not available when the OFT investigates suspected infringements of Article 81 or Article 82 on its own behalf. Primarily, the officers will not only be able to ask employees of the undertaking under inspection for explanations of documents but also of **facts** relating to the subject matter and purpose of the inspection[39]. The authorisation will identify the officers, the subject matter and purpose of the investigation and draw attention to the penalties which an undertaking may incur in connection with the inspection under the relevant provision of Community law[40].

9.5 When **assisting** the European Commission with an inspection of non-business premises, the OFT must obtain a warrant **before** any inspection can be carried out. The warrant will authorise officers of the OFT and officials of the European Commission to enter the non-business premises and may also authorise a power to search for books and records that the officials have power to examine, as well as the use of such force as is reasonably necessary for the purpose. When assisting the European Commission in this way, the officers of the OFT have the same powers as an official authorised by the European Commission[41].

9.6 Any warrant obtained by the OFT in connection with an investigation by the European Commission must indicate the subject matter and purpose of the investigation and the nature of the offence for obstruction described in paragraph 9.10. The warrant may also authorise other persons to accompany the authorised officers on the inspection, such as computer technicians or industry experts.

9.7 The range of documents that can benefit from legal professional privilege in inspections conducted **to assist** the European Commission is narrower than when the OFT is investigating suspected infringements of Article 81 or Article 82 on its own behalf or on behalf of another NCA. The European Court has recognised that correspondence between a client and an external legal adviser, entitled to practise in one of the Member States, is subject to legal professional privilege where: (i) the

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[38] Section 62B(1).
[39] Article 20(2)(e) of the Modernisation Regulation.
[40] Article 23(1)(c) (fines) and Article 24(1)(e) (periodic penalty payments) of the Modernisation Regulation.
[41] Article 21(4) of the Modernisation Regulation.

correspondence follows the initiation of proceedings by the European Commission and concerns the defence of the client; or (ii) the correspondence existed before the initiation of proceedings but is closely linked with the subject-matter of the proceedings. Correspondence between a client and an external legal adviser who is not entitled to practise in one of the Member States[42] or between a client and an in-house legal adviser (unless the in-house legal adviser is simply reporting the statement of an external legal adviser) is not recognised by the European Court as being protected by legal professional privilege.

9.8 Where an inspection is being conducted to assist the European Commission, legal professional privilege can be claimed only for documents that fall within the category of correspondence that the European Court has recognised as being subject to legal professional privilege. In order to claim legal professional privilege for certain documents during an inspection the occupier must make a case to the European Commission demonstrating why the documents are covered by legal professional privilege. If the European Commission rejects the occupier's arguments, the European Commission may adopt a decision requiring the documents to be handed over. The occupier can challenge this decision in the European Court.

9.9 Where an inspection is being conducted by the OFT **on behalf of** the European Commission (under section 63 of the Act), the United Kingdom rules on legal professional privilege will apply.

9.10 A person will be guilty of an offence if they intentionally obstruct any person in the exercise of their powers under a warrant issued in relation to a European Commission investigation relating to Article 81 or 82. The sanction is a fine of up to the statutory maximum on summary conviction or an unlimited fine and/or a maximum of two years' imprisonment on conviction on indictment.

[42] The European Commission has indicated that such correspondence may be protected if suitable reciprocity agreements are negotiated.

10 POWER TO ASSIST NATIONAL COMPETITION AUTHORITIES OF EC MEMBER STATES

10.1 The Modernisation Regulation enables the NCAs of Member States to investigate suspected infringements of Article 81 and Article 82 on behalf of each other.

10.2 Under Part 2A of the Act, the OFT may carry out an inspection or other fact-finding measure in the United Kingdom on behalf of an NCA of another Member State in order to assist it in establishing whether there has been an infringement of Article 81 or 82.

10.3 In such circumstances the OFT will apply similar powers of investigation to those it uses to investigate suspected infringements of Article 81 and 82 under Part I of the Act. This means that where there are reasonable grounds for suspecting that an agreement falls within Article 81 or that the prohibition in Article 82 has been infringed, the OFT will have the power to:

- require the production of specified documents and information (see Part 3 above)
- enter business premises without a warrant (see Part 4 above), and
- enter and search business or domestic premises with a warrant (see Part 5 above).

10.4 These powers of investigation are not available to the Regulators; however, they may participate in inspections carried out by the OFT on behalf of other NCAs if the industry being investigated falls within their area of expertise.

10.5 These powers of investigation are subject to the same restrictions concerning legal professional privilege and self-incrimination that are described in Part 6. Individuals who fail to comply with such investigations risk committing the same offences and face the same possible sanctions as described in Part 7.

10.6 Although other NCAs do not have any formal powers of investigation within the United Kingdom, officers of other NCAs may be authorised to accompany the OFT on an inspection where the OFT uses its power to enter premises under a warrant, provided that the warrant identifies them[43].

[43] Sections 65G(4) and 65H(4).

ANNEXURE C

OFFICE OF FAIR TRADING

Enforcement

Incorporating the Office of Fair Trading's guidance as to the circumstances in which it may be appropriate to accept commitments

Draft competition law guideline for consultation

April 2004

OFT407a

Articles 81 and 82 of the EC Treaty and the Competition Act 1998 are applied and enforced in the United Kingdom by the Office of Fair Trading (the OFT). In relation to the regulated sectors these provisions are applied and enforced, concurrently with the OFT, by the regulators for communications matters, gas, electricity, water and sewerage, railway and air traffic services (under section 54 and schedule 10 of the Competition Act 1998) (the Regulators). Throughout the guidelines, references to the OFT should be taken to include the Regulators in relation to their respective industries, unless otherwise specified.

The following are Regulators:

- the Office of Communications (OFCOM)
- the Gas and Electricity Markets Authority (OFGEM)
- the Northern Ireland Authority for Energy Regulation (OFREG NI)
- the Director General of Water Services (OFWAT)
- the Rail Regulator[1] (ORR), and
- the Civil Aviation Authority (CAA).

This publication is divided into a guideline and, in the annexe, the OFT's guidance as to the circumstances in which it may be appropriate to accept commitments.

The guideline provides general advice and information about the application and enforcement by the OFT of Articles 81 and 82 of the EC Treaty and the Chapter I and II prohibitions contained in the Competition Act 1998. It is intended to explain these provisions to those who are likely to be affected by them and to indicate how the OFT expects them to operate. Further information on how the OFT has applied and enforced competition law in particular cases may be found in the OFT's decisions, as available on its website from time to time.

[1] This will change to the Office of Rail Regulation on 5 July 2004.

The guideline is not a substitute for the EC Treaty nor for regulations made and notices provided under it. Neither is it a substitute for the Competition Act 1998 and the regulations and orders made under it. It should be read in conjunction with these legal instruments, Community case law and United Kingdom case law. Anyone in doubt about how they may be affected by the EC Treaty and the Competition Act 1998 should seek legal advice.

As regards the guidance contained in the annexe, the OFT is required to have regard to this guidance in considering whether to accept any commitments offered to it. It is issued in performance of the statutory obligation placed on the OFT (but not the Regulators) by section 31D(1) of the Act to prepare and publish guidance as to the circumstances in which it may be appropriate to accept commitments.

CONTENTS

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1 INTRODUCTION

1.1 The EC Treaty[2] and the Competition Act 1998 (the Act) both prohibit, in certain circumstances, agreements[3] and conduct which prevent, restrict or distort competition. EC Regulation 1/2003 (the Modernisation Regulation)[4] allows national competition authorities of the Member States (NCAs) and the courts of the Member States to apply and enforce Articles 81 and 82 of the EC Treaty (Article 81 and Article 82 respectively). The Act gives the Office of Fair Trading (the OFT) powers to enforce both the Chapter I and Chapter II prohibitions of the Act and Article 81 and Article 82.

1.2 The OFT's enforcement powers are set out in sections 25-44 of the Act. This guideline describes the power of the OFT:

- to give directions to bring an infringement to an end (Part 2)
- to give interim measures directions during an investigation (Part 3)
- to accept binding commitments offered to it (Part 4), and
- to impose financial penalties on undertakings for infringing Article 81, Article 82, the Chapter I and/or Chapter II prohibitions (Part 5).

1.3 Private remedies arising from breach of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions are described in Part 6 of this guideline. The powers of investigation of the OFT under the Act are described in the competition law guideline *Powers of investigation* (OFT404).

1.4 The Act requires the OFT (not including the Regulators) to prepare and publish guidance as to the circumstances in which it may be appropriate to accept binding commitments. The OFT must have regard to the guidance for the time being in force. This guidance is summarised in Part 4 below and appears in full as an annexe to this guideline.

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[2] The Treaty of Rome, establishing the European Community, as consolidated by the Treaty of Amsterdam.

[3] References in this guideline to **'agreements'** should, unless otherwise stated or the context demands it, be taken to include decisions by associations of undertakings and concerted practices.

[4] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (OJ L1, 4.1.03, p 1).

2 DIRECTIONS

2.1 The Act provides that the OFT may give such directions as it considers appropriate to bring an infringement to an end where the OFT has made a decision that Article 81, Article 82, the Chapter I and/or Chapter II prohibitions has or have been infringed. In each case where an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions is alleged, the OFT must prove the infringement. A decision by the OFT that a person has infringed the Chapter I prohibition and/or the Chapter II prohibition must be based on strong and compelling evidence[5]. Similarly, the OFT will not reach a decision that a person has infringed Article 81 and/or Article 82 except on the basis of strong and compelling evidence.

2.2 The directions may be given to such person(s) as the OFT considers appropriate, which includes individuals and undertakings[6]. The OFT is not limited to giving directions to the infringing parties. For example, directions may be addressed to the parent company which, though not the actual instigator of the infringement, has a subsidiary which is the immediate party to the infringement.

2.3 Directions may in particular require the person concerned to modify the agreement or conduct, or to terminate the agreement or cease the conduct in question. Directions may require positive action, such as informing third parties that an infringement has been brought to an end and reporting back periodically to the OFT on certain matters such as prices charged. In some circumstances, the directions appropriate to bring an infringement to an end may be (or may include) directions requiring an undertaking to make structural changes to its business.

Procedure

2.4 The directions must be in writing and may be given to such person(s) as the OFT considers appropriate. They are likely to form part of the infringement decision in cases where the decision and the directions are addressed to the same person. If the OFT proposes to make an

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[5] See NAPP Pharmaceutical Holdings Limited v Director General of Fair Trading [2002] CAT 1 at [105]–[113], [2002] CompAR 13 ('**Napp**').

[6] See paragraph 5.41 below for further detail on the definition of '**undertaking**'.

infringement decision, it will send the party or parties a written statement setting out the facts on which the OFT relies, the matters to which it has taken objection, the action it proposes to take and the reasons for it. The OFT's Rules[7] provide that the OFT must allow the person receiving the notice an opportunity to make written representations to it. The person receiving the notice may request a meeting with officials of the OFT to make oral representations to elaborate on the written representations already made in this regard.

2.5 The OFT's Rules also provide that the OFT must give the party or parties or their authorised representative a reasonable opportunity to inspect the documents in the OFT's file relating to the proposed decision[8]. The OFT may withhold any documents to the extent to which they contain confidential information and may withhold the OFT's internal documents.

2.6 Any directions given by the OFT will set out the facts on which the direction is based and the reasons for it[9]. The directions will be published on the register maintained by the OFT, which is open to public inspection on the OFT's website.

2.7 Directions can be appealed to the Competition Appeal Tribunal (the CAT). The making of an appeal will not suspend the effect of the direction. The rules of the CAT provide, however, that the CAT can make an interim order to suspend the effect of any direction which is the subject of an appeal before it[10].

Enforcement of directions

2.8 In most cases directions will have immediate effect. In some cases the OFT may allow the undertakings a period of time within which to comply with a direction.

2.9 The OFT may apply to the court for an order requiring compliance with a direction within a specified time limit if a person fails to comply with it without reasonable excuse. The OFT will actively seek to enforce directions in the courts. The court can require the person in default, or

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[7] The Competition Act 1998 (Office of Fair Trading's Rules) Order 2004 (SI 2004/[ ]) (**'the OFT's Rules'**), rule 5.
[8] OFT's Rules, rule 5.
[9] OFT's Rules, rule 8.
[10] The Competition Appeal Tribunal Rules 2003 (SI 2003/1372) (**'the CAT Rules'**), rule 61.

any officer of an undertaking who is responsible for the default, to pay the costs of obtaining the order. If a direction relates to the management or administration of an undertaking the order can compel the undertaking or any of its officers to comply with it. Any person who fails to comply with an order enforcing a direction will be in contempt of court. The sanction for contempt of court is a fine or imprisonment.

3 INTERIM MEASURES DIRECTIONS

3.1 The Act provides that the OFT may give interim measures directions pending its final decision as to whether or not there has been an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions. Interim measures directions will not affect the final decision.

3.2 The Modernisation Regulation gives the OFT the power to order interim measures directions when applying Article 81 and/or Article 82 in particular cases[11], but the test for whether to give interim measures directions is a matter determined by national law.

3.3 The Act provides that the OFT may give interim measures directions before it has completed its investigation of the suspected infringement if:

- the OFT has begun an investigation under section 25 of the Act and not completed it (but only so long as the OFT has power under section 25 to conduct that investigation), and
- the OFT considers that it is necessary to act urgently either to prevent serious, irreparable damage to a particular person or category of persons, or to protect the public interest.

3.4 The circumstances in which the OFT has power to conduct an investigation under section 25 of the Act are described in the competition law guideline *Powers of investigation* (OFT404). Broadly the OFT has this power where it has reasonable grounds to suspect an agreement which falls within Article 81 or the Chapter I prohibition, or conduct which infringes Article 82 or the Chapter II prohibition.

3.5 What constitutes serious damage is a question of fact and will depend upon the circumstances of each case. However, damage may be serious where a particular person or category of persons may suffer considerable competitive disadvantage likely to have a lasting effect on their position. Serious damage is likely to include significant financial loss to a person (to be assessed with reference to that person's size or financial resources as well as the proportion of the loss in relation to the person's total

[11] Article 5 of the Modernisation Regulation.

revenue), and significant damage to the goodwill or reputation of a person might also constitute serious damage.

3.6 Irreparable does not mean that a person must be threatened with insolvency, though this will generally suffice. Less extreme forms of serious damage may still be irreparable, in so far as they cannot be remedied by later intervention. 'Serious' and 'irreparable' damage are cumulative, though inter-related, requirements. Thus, serious damage which is not irreparable will not suffice. The serious, irreparable damage must be shown to result from the alleged anti-competitive behaviour.

3.7 The OFT may consider that it is necessary to act urgently to protect the public interest, for example, to prevent damage being caused to a particular industry or to consumers as a result of the suspected infringement. It may also take action to prevent damage to competition more generally.

3.8 Interim measures directions may be given by the OFT on its own initiative or after receiving a request provided that the tests in paragraph 3.3 above are satisfied and that the circumstances in paragraph 3.9 below do not apply. Any person requesting an interim measures direction should provide as much evidence as possible, demonstrating that the alleged infringement is causing serious, irreparable damage or that it is necessary that the OFT act to protect the public interest. Such a request should also indicate as precisely as possible the nature of the interim measure sought.

3.9 Where the OFT's investigation under section 25 of the Act concerns an agreement, the OFT may not give interim measures directions where a party to the agreement has produced evidence to the OFT that, on the balance of probabilities, satisfies the OFT that the agreement is exempt from the Chapter I prohibition as a result of section 9(1) of the Act, or that the prohibition in Article 81(1) is inapplicable because it satisfies the conditions in Article 81(3), as appropriate.[12]

3.10 The OFT may give such interim measures directions as it considers appropriate. The OFT may in particular require the person concerned to

[12] For more detail on section 9(1) of the Act and Article 81(3) see the competition law guideline *Article 81 and the Chapter I prohibition* (OFT401).

terminate the agreement or cease the conduct in question, or to modify the agreement or conduct.

3.11 When the investigation is complete and the OFT has decided that an infringement has taken place, it may replace the interim measures direction with a direction described in Part 2 above. An interim measures direction may also, in an appropriate case, be replaced by the acceptance of binding commitments (see Part 4 below). Otherwise, an interim measures direction has effect until the OFT no longer has power under section 25 to conduct the investigation or until it has completed its investigation into the matter.

Procedure

3.12 Before giving an interim measures direction the OFT must give written notice to the person to whom it proposes to give the direction, indicating the nature of the direction it proposes to give and the reasons for deciding to give it. The OFT must allow the person receiving the notice an opportunity to make written representations to it. The person receiving the notice may request a meeting with officials of the OFT to make oral representations to elaborate on written representations already made in this regard.

3.13 The person who receives written notice from the OFT about the proposed interim measures direction may inspect the OFT's file on the case. The OFT's Rules provide that the OFT must give such a person or their authorised representative a reasonable opportunity to inspect the documents in the OFT's file relating to the proposed direction[13]. The OFT may withhold any documents to the extent to which they contain confidential information and may withhold the OFT's internal documents.

3.14 The interim measures direction will be published on the register maintained by the OFT, which is open to public inspection on the OFT's website. The OFT may also publish the interim measures direction in an appropriate trade journal.

[13] OFT's Rules, rule 9.

3.15 An interim measures direction can be appealed to the CAT. The making of an appeal will not suspend the effect of the interim measures direction, but the CAT may suspend its effect by interim order[14].

[14] See footnote 10 above.

Enforcement of interim measures directions

3.16 Interim measures directions can be enforced following the procedure set out in paragraph 2.9 above.

Assurances in lieu of interim measures directions

3.17 The OFT may accept informal interim assurances offered by the person(s) concerned where it is satisfied that these will prevent any harm which might otherwise form the basis for imposition of an interim measures direction.

3.18 One of the prerequisites for an interim remedy is that it is necessary to act as a matter of urgency. The ability to accept informal interim assurances in appropriate circumstances helps facilitate quick action by the OFT.

3.19 The OFT may replace informal interim assurances by an interim measures direction.

3.20 When an investigation is complete and the OFT has decided that an infringement has taken place, it may replace any informal interim assurances with a direction described in Part 2 above. In an appropriate case, the OFT may also replace interim assurances by accepting binding commitments (see Part 4 below).

4 COMMITMENTS

4.1 The Act gives the OFT the power to accept binding commitments offered to it by a person or persons if it is satisfied that those commitments meet its competition concerns. Exercise of this power allows the OFT to terminate its investigation into an alleged infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions.

4.2 The Act requires the OFT (not including the Regulators) to prepare and publish guidance as to the circumstances in which it may be appropriate to accept binding commitments. The OFT must have regard to the guidance for the time being in force when considering whether to accept any commitments offered to it. Although there is no equivalent statutory obligation on the Regulators to publish guidance as to the circumstances in which it may be appropriate to accept binding commitments, the Regulators are required to have regard to the guidance for the time being in force when considering whether to accept any commitments offered to them. The guidance was approved by the Secretary of State (as required under section 31D(4) of the Act) on [date to be inserted]. It is summarised below and appears in full as an annexe to this guideline.

4.3 The decision whether to accept binding commitments is at the discretion of the OFT. The OFT is likely to consider it appropriate to accept binding commitments only in cases where:

- the competition concerns are readily identifiable
- the competition concerns are fully addressed by the commitments offered, and
- the proposed commitments are capable of being implemented effectively and, if necessary, within a short period of time.

4.4 The OFT will not, other than in very exceptional circumstances,[15] accept binding commitments in cases involving secret cartels between competitors which include:

- price-fixing

[15] For example cases which might feature the restrictions listed in paragraph 4.4 but where the OFT considers that the administrative cost involved in continuing the investigation and proceeding to a final decision would outweigh the benefits.

- bid-rigging (collusive tendering)
- establishing output restrictions or quotas
- sharing markets, and/or
- dividing markets.

Nor will the OFT accept binding commitments in cases involving serious abuse of a dominant position[16].

4.5 The OFT will not accept binding commitments in circumstances:

- where compliance with and the effectiveness of any binding commitments would be difficult to discern, and/or
- where the OFT considers that not to complete its investigation and make a decision would undermine deterrence.

4.6 Commitments may be structural or behavioural in nature, or a combination of both. For example, commitments might involve a person agreeing to cease or modify its conduct in a particular area, terminating an exclusive arrangement, removing a particular clause from an agreement, withdrawing from a particular activity, licensing specific assets or even divesting itself of a part of its business.

4.7 Once binding commitments have been accepted, the OFT will terminate its investigation into the aspects of the alleged infringement addressed by the commitments (see further paragraphs 4.9 and 4.10 below). The commitments will have the same force and effect as if they were directions made by the OFT (see Part 2 above). A decision by the OFT accepting binding commitments will state that the commitments offered by the undertaking meet the OFT's competition concerns, but will not include any statement as to the legality or otherwise of the agreement or

[16] It is the OFT's assessment of the seriousness of an abuse and its effect on competition which will be taken into account in determining whether commitments are appropriate in a particular case. When making its assessment, the OFT will consider a number of factors, including the nature of the product, the structure of the market, the market share(s) of the undertaking(s) involved, entry conditions and the effect on competitors and third parties. The damage caused to consumers whether directly or indirectly will also be an important consideration. This assessment will be made on a case by case basis, taking account of all the circumstances of the case. However, as a general rule, the OFT will regard predatory pricing as a serious abuse.

conduct either prior to the acceptance of the commitments or once the commitments are in place.

4.8 Binding commitments will generally be adopted for a specified period of time. They are treated as released on the expiry of this period.

4.9 Once binding commitments have been accepted in respect of an agreement or conduct, the OFT may not continue an investigation, make an infringement decision or give interim measures directions in respect of that agreement or conduct unless it has:

- reasonable grounds for believing that there has been a material change of circumstances since the commitments were accepted
- reasonable grounds for suspecting that a person has failed to adhere to one or more of the terms of the binding commitments, or
- reasonable grounds for suspecting that information which led it to accept the binding commitments was incomplete, false or misleading in a material particular[17].

If such a decision is made or the OFT gives such directions, the person will be considered released from its binding commitments as from the date of that decision.

4.10 However, the OFT is not prevented from taking action in relation to competition concerns other than those addressed by the commitments it has accepted. This may arise, for example, where an agreement or conduct raises a number of competition concerns, or where different aspects of an agreement or conduct raise different competition concerns. The OFT may accept commitments in respect of some of its competition concerns and may continue its investigation in respect of other competition concerns, even where they arise out of the same agreement or conduct.

4.11 Whilst binding commitments are in force, the OFT may review their effectiveness and take such action as regards variation or release as it deems appropriate.

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[17] Section 44 of the Act provides that it is a criminal offence knowing or recklessly to provide materially false or misleading information. See the competition law guideline *Powers of investigation* (OFT404) for further discussion of offences.

4.12 Where the OFT has accepted binding commitments it may, for the purposes of addressing the competition concerns which it identified at the time of such acceptance or for the purposes of addressing any new competition concerns it has identified, consider it appropriate to accept a variation of the commitments or commitments in substitution for them.

4.13 If different competition concerns are identified by the OFT, the appropriateness of accepting varied or substitute commitments will take into account the considerations in paragraphs 4.3 to 4.5 above.

4.14 The OFT may consider it appropriate to release binding commitments where:

- it is requested to do so by the person or persons who gave the commitments, or
- the competition concerns identified by it at the time of their acceptance or variation no longer arise.

4.15 Where the OFT is reviewing or has reviewed the effectiveness of binding commitments it must, whenever requested to do so by the Secretary of State, prepare a report of its findings. Such report will be given to the Secretary of State and published.

Procedure

4.16 There is no requirement for a person to offer binding commitments to the OFT at any time.

4.17 A person or persons may offer binding commitments to the OFT at any time during the course of an investigation and until a decision is made. However, the OFT is unlikely to consider it appropriate to accept commitments offered at a very late stage in its investigation (for example, after the OFT has considered representations in relation to its statement of objections).

4.18 If a person or persons wish to offer commitments prior to the issue of the OFT's statement of objections and the OFT considers that the case is one in which commitments may be appropriate, the OFT will issue a summary of its competition concerns. Such summary is not a replacement for a statement of objections. It will set out the OFT's competition concerns and a summary of the main facts on which those

concerns are based. However, it will not generally include detail of the source of the facts on which the OFT relies.

4.19 Once commitments have been offered, the OFT may enter into discussions with the person or persons in order to reach agreement as to the form and content of commitments which would be acceptable to the OFT.

4.20 The fact that the OFT has issued a summary of its concerns and/or entered into discussions on the form and content of commitments does not preclude the OFT from making a decision in relation to the agreement or conduct if acceptable commitments are not agreed or if other factors mean that it is not appropriate to accept commitments.

4.21 Where the OFT proposes to accept commitments, it will give notice to such persons as it considers likely to be affected by the commitments providing a summary of the case and setting out the proposed commitments and stating the purpose of the commitments and the way in which they meet the OFT's competition concerns. Interested third parties will have an opportunity to make representations within a time limit fixed by the OFT (being not less than 11 working days starting with the date the notice is given).

4.22 Following this consultation period, if the OFT intends to accept the commitments with any material modifications, it will give notice to such persons as it considers likely to be affected by the commitments of the proposed modifications and the reasons for them. Interested third parties will have an opportunity to make representations on the proposed modifications within a time limit fixed by the OFT (being not less than six working days starting with the date the notice is given).

4.23 Once accepted, binding commitments will be published by the OFT. The procedure in paragraphs 4.21 and 4.22 above will also apply to any variation of binding commitments. Before releasing a person or persons from any binding commitments the OFT will give notice of the proposed release, and the reasons for it, to such persons as it considers likely to be affected and send a copy of the notice to the person or persons who gave the commitments. Interested third parties will have an opportunity to make representations within a time limit fixed by the OFT (being not less than 11 working days starting with the date the notice is given). After having released commitments, the OFT will publish the release and

send a copy of the release to the person or persons who gave the commitments.

4.24 In publishing information relating to binding commitments, the OFT will have regard to the need to exclude from disclosure (so far as practicable):

- commercial information, disclosure of which the OFT considers might significantly harm the legitimate business interests of the undertaking to which it relates
- information relating to the private affairs of an individual, disclosure of which the OFT considers might significantly harm the individual' s interests, and
- any information disclosure of which the OFT considers is contrary to the public interest.

This is in accordance with the provisions of Part 9 of the Enterprise Act.

4.25 Any sufficiently interested person may seek to have a commitments decision reviewed by the CAT. For this purpose, a commitments decision is a decision by the OFT to accept, vary or release commitments (other than a variation which is not material in any respect) or a decision not to release commitments pursuant to a request made by the person or persons who gave the commitments.

4.26 On review, the CAT may:

- dismiss the application for review or quash the whole or part of the commitments decision to which it relates, and
- where it quashes the whole or part of that decision, refer the matter back to the OFT with a direction to reconsider and make a new decision in accordance with the ruling of the CAT.

4.27 Third parties may also pursue private actions before the courts in relation to agreements or conduct they consider constitute infringements of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions, notwithstanding any binding commitments accepted by the OFT.

Enforcement of binding commitments

4.28 Binding commitments are enforceable by the OFT in the same way as directions (see paragraph 2.9 above).

PENALTIES

General powers

5.1 The Act provides that the OFT may impose a financial penalty on an undertaking which has intentionally or negligently committed an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions. The amount of the penalty imposed may be up to 10 per cent of the undertaking's worldwide turnover[18]. It is for the OFT to determine whether a financial penalty should be imposed. The OFT can impose penalties for infringements that have already stopped as well as for ongoing infringements.

5.2 The OFT uses this power to impose penalties on infringing undertakings which reflect the seriousness of the infringement and constitute a serious and effective deterrent, both to the undertaking concerned and to other undertakings which might be considering activities contrary to Article 81, Article 82, the Chapter I and/or Chapter II prohibitions. Therefore, subject to the maximum penalty of 10 per cent of an undertaking's worldwide turnover, the OFT may, where appropriate, increase levels of penalties to ensure that deterrence is achieved[19].

5.3 In cases where an undertaking has committed an infringement of both Article 81 and/or Article 82 and the Chapter I and/or Chapter II prohibition, the OFT may impose penalties in respect of the infringements of both Article 81 and/or Article 82 and the Chapter I and/or Chapter II prohibition. However, when imposing penalties under Article 81, the OFT will, as a matter of policy, take into account any penalties imposed under the Chapter I prohibition in respect of the same aspects of the same agreements. Likewise, when imposing penalties under Article 82, the OFT will, as a matter of policy, take into account any penalties imposed under the Chapter II prohibition in respect of the same conduct.

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[18] See section 36(8) of the Act and the Competition Act 1998 (Determination of Turnover for Penalties) Order 2000 (SI 2000/309) as amended by the Competition Act 1998 (Determination of Turnover for Penalties) (Amendment) Order 2004 (SI 2004/[ ]).
[19] See Napp at [502].

Intentionally or negligently

5.4 Before exercising the power to impose a financial penalty, the OFT must be satisfied, as a threshold condition, that the infringement has been committed intentionally or negligently. However, it does not, for the purposes of crossing that threshold, have to determine specifically which it was, provided that it is satisfied that the infringement was **either** intentional or negligent (although it may well have to do so at a subsequent stage of its appraisal)[20].

5.5 For intention or negligence to be found it is not necessary for there to have been action by, or even knowledge on the part of, the partners or principal managers of the undertaking concerned; action by a person who can act on behalf of the undertaking suffices.

5.6 The OFT may consider the existence of past Restrictive Practice Court orders made against, and undertakings in lieu given by, an undertaking when considering whether or not an infringement of Article 81 and/or the Chapter I prohibition by similar anti-competitive activities of that undertaking was committed intentionally or negligently.

5.7 The OFT may also consider binding commitments given by an undertaking when considering whether or not an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions by similar anti-competitive activities of that undertaking was committed intentionally or negligently.

5.8 The fact that a particular type of agreement or conduct has not previously been found to be in breach of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions does not mean that the infringement cannot be committed intentionally or negligently.

Intention

5.9 The circumstances in which the OFT might find that an infringement has been committed intentionally include the following:

- the agreement or conduct has as its object the restriction of competition

[20] Section 36(3) of the Act. See also Napp at [453]-[455] and Aberdeen Journals Limited v The Office of Fair Trading [2003] CAT 11 ('Aberdeen Journals (No.2)') at [484].

- the undertaking in question is aware that its actions will be, or are reasonably likely to be, restrictive of competition but still wants, or is prepared, to carry them out, or
- the undertaking could not have been unaware that its agreement or conduct would have the effect of restricting competition, even if it did not know that it would infringe Article 81, Article 82, the Chapter I and/or Chapter II prohibitions[21].

5.10 The intention (or negligence, referred to below) relates to the facts, not the law. Ignorance or a mistake of law (i.e. ignorance that the relevant agreement or conduct is an infringement) is thus no bar to a finding of intentional infringement.

5.11 In establishing whether or not there is intention, the OFT may consider internal documents generated by the undertakings in question. The OFT may regard deliberate concealment of an agreement or practice by the parties as strong evidence of an intentional infringement. It may be inferred that an infringement has been committed intentionally where consequences giving rise to an infringement are plainly foreseeable from the pursuit of a particular policy by an undertaking[22].

Negligence

5.12 The OFT is likely to find that an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions has been committed negligently where an undertaking ought to have known that its agreement or conduct would result in a restriction or distortion of competition[23].

Involuntary infringement

5.13 Where an undertaking participates in an infringement under pressure, it may still be held to have acted intentionally or negligently, although, depending on the circumstances, the penalty may be reduced[24].

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[21] See Napp at [456] and Aberdeen Journals (No.2) at [485]-[488].
[22] See Napp at [456] and Aberdeen Journals (No.2) at [485]-[488].
[23] See Napp at [457]. And see also Case 27/76 United Brands Co and United Brands Continental BV v Commission [1978] 1 CMLR 429 at paragraphs 298-301, [1977] ECR 207.
[24] See the *OFT's Guidance as to the appropriate amount of a penalty* (OFT423).

Turnover

5.14 The definition of turnover for the purposes of determining the maximum financial penalty of 10 per cent of worldwide turnover that can be imposed is set out in an order made by the Secretary of State pursuant to section 36(8) of the Act[25]. A financial penalty imposed by the OFT under section 36 of the Act will be calculated following a five step approach. Details of each of these steps and the factors to which the OFT has regard are set out in the *OFT's Guidance as to the appropriate amount of a penalty* (OFT423) (and see also paragraphs 5.28 to 5.32 below).

Tax deductibility of penalties

5.15 It is the view of the Inland Revenue that financial penalties imposed under the Act will not be deductible in computing trading profits for tax purposes[26]. This is because civil or criminal penalties imposed by or under the authority of an Act of Parliament are not deductible: they are **'losses not connected with or arising out of the trade'** and so not deductible by virtue of section 74(1)(e) of the Income and Corporation Taxes Act 1988.

Limited immunity for 'small agreements' and 'conduct of minor significance'

5.16 In order to avoid the prohibition regime being unduly burdensome on small businesses, the Act provides limited immunity from financial penalties for **'small agreements'** in relation to infringements of the Chapter I prohibition and for **'conduct of minor significance'** in relation to infringements of the Chapter II prohibition. This immunity does not apply to any infringements of Article 81 or Article 82 or to infringements of the Chapter I prohibition which are price-fixing agreements.

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[25] The Competition Act 1998 (Determination of Turnover for Penalties) Order 2000 (SI 2000/309) as amended by the Competition Act 1998 (Determination of Turnover for Penalties) (Amendment) Order 2004 (SI 2004/[ ]).

[26] Commissioners of Inland Revenue v Alexander von Glehn & Co Ltd (12 TC 232).

5.17 The term 'small agreements' relates to agreements between undertakings whose combined annual turnover does not exceed £20 million[27]. Conduct will be considered to be of minor significance if the annual turnover of the undertaking concerned does not exceed £50 million.

5.18 Undertakings will benefit from immunity from financial penalties for infringement of the Chapter I prohibition or Chapter II prohibition, as appropriate, if the OFT is satisfied that they acted on the reasonable assumption that on the facts they qualified for the limited immunity for 'small agreements' or 'conduct of minor significance'.

5.19 The immunity applies only to financial penalties: an anti-competitive agreement or abusive conduct by such undertakings is still an infringement, and consequently the OFT may take other enforcement action, and the immunity does not prevent third parties from claiming damages for the loss caused by such an agreement or conduct (see further paragraph 6.1 below).

5.20 The OFT may still investigate small agreements or conduct of minor significance and can decide to withdraw the immunity from financial penalties if, having investigated the agreement or conduct, it considers that it is likely to infringe the Chapter I prohibition and/or the Chapter II prohibition.

5.21 Where the OFT has withdrawn the immunity from penalties for infringement of the Chapter I prohibition or the Chapter II prohibition, it must give written notice of its decision to the person or persons from whom the immunity has been withdrawn. The notice will specify the date on which the withdrawal of immunity is to take effect. When determining that date, the OFT must have regard to the amount of time which the person or persons affected are likely to need in order to secure that there is no further infringement of the Chapter I prohibition or the Chapter II prohibition, as the case may be. That date must follow the date of the OFT's decision.

[27] Full details of how turnover is to be calculated can be found in the Competition Act 1998 (Small Agreements and Conduct of Minor Significance) Regulations 2000 (SI 2000/262).

EC block exemption regulations

5.22 The European Commission may adopt block exemption regulations so that particular categories of agreement which it considers satisfy the conditions in Article 81(3) are not prohibited under Article 81[28]. Where an agreement is covered by an EC block exemption regulation[29], the parties to the restrictive agreement are relieved of the burden of showing that their agreement satisfies the conditions in Article 81(3).

5.23 A parallel exemption under the Act applies to an agreement which is covered by an EC block exemption regulation, or which would be covered by an EC block exemption regulation if the agreement had an effect on trade between Member States. These types of agreement are not prohibited under the Act. In certain circumstances, the OFT may impose conditions on a parallel exemption, or vary or cancel the parallel exemption, following procedures set out in the OFT's Rules[30].

5.24 The European Commission may, under Article 29(1) of the Modernisation Regulation, withdraw the benefit of any EC block exemption regulation if it finds that in a particular case the agreement in question has effects that are incompatible with Article 81(3).

5.25 The OFT may also, under Article 29(2) of the Modernisation Regulation, withdraw the benefit of any EC block exemption regulation in a particular case from any agreements if the following conditions are met:

- the territory of the United Kingdom, or a part of it, has all the characteristics of a distinct geographic market, and

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[28] The European Commission may only issue a block exemption regulation where it has been empowered to do so. For instance, Council Regulation (EEC) No 19/65 allows the European Commission to adopt block exemption regulations in respect of vertical agreements and industrial property rights.

[29] EC block exemption regulations in force include: Commission Regulation (EC) No 2658/2000 on the application of Article 81(3) of the Treaty to categories of specialisation agreements; Commission Regulation (EC) No 2659/2000 on the application of Article 81(3) of the Treaty to categories of research and development agreements; Commission Regulation (EC) No 2790/1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices; Commission Regulation (EC) No 1400/2002 on the application of Article 81(3) to categories of vertical agreements and concerted practices in the motor vehicle sector; and Commission Regulation (EC) No [ ]/2004 on the application of Article 81(3) of the Treaty to categories of technology transfer agreements.

[30] OFT's Rules, rule 12.

- the agreements in question have effects that are incompatible with Article 81(3) in the territory of the United Kingdom.

In such circumstances, the OFT will follow the procedures set out in the OFT's Rules[31]. For further details see the competition law guideline *Vertical agreements* (OFT419).

5.26 The United Kingdom courts have no power to withdraw the benefits of an EC block exemption regulation.

5.27 Agreements benefiting from a block exemption regulation or a parallel exemption are still subject to Article 82 and the Chapter II prohibition in so far as they involve undertakings in a dominant position. An infringement of Article 82 and/or the Chapter II prohibition may be found without first withdrawing the benefit of the relevant block exemption regulation[32].

Amount of a penalty

5.28 Section 38 of the Act places an obligation on the OFT to prepare and publish guidance as to the appropriate amount of any penalty, including guidance as to the circumstances in which, in determining a penalty, the OFT may take into account the effects of an infringement in another Member State (see paragraph 5.30 below). The purpose of such guidance is to inform and guide businesses on the level of penalties. The guidance explains the steps taken and the factors to which the OFT has regard when setting the level of a penalty[33]. The obligation to prepare and publish guidance is on the OFT alone, but the OFT and the Regulators must have regard to the guidance when setting the level of a penalty.

5.29 In brief, a financial penalty imposed by the OFT for an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions will be calculated following a five step approach:

- step 1 – calculation of the starting point having regard to the seriousness of the infringement and the 'relevant turnover' of the undertaking

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[31] OFT's Rules, rule 13.
[32] Case T-51/89 Tetra Pak Rausing SA v Commission [1990] ECR II-309, [1991] 4 CMLR 334.
[33] See the *OFT's Guidance as to the appropriate amount of a penalty* (OFT423).

- step 2 – adjustment for duration
- step 3 – adjustment for other factors
- step 4 – adjustment for further aggravating or mitigating factors
- step 5 – adjustment if the maximum penalty of 10 per cent of the worldwide turnover of the undertaking is exceeded and to avoid double jeopardy.

Effects in other Member States

5.30 In cases concerning infringements of Article 81 and/or Article 82, the OFT may take into account the effects in another Member State in calculating the penalty to be imposed, provided the express consent of the relevant Member State or NCA, as appropriate, is given in each particular case.

5.31 If a penalty or fine has already been imposed by the European Commission or by a court or other body in another Member State in respect of an agreement or conduct, the OFT must take that penalty or fine into account when setting the amount of any penalty in relation to that agreement or conduct[34]. This is to ensure that where an anti-competitive agreement or conduct is subject to proceedings resulting in a penalty or fine in another Member State, an undertaking will not be penalised again in the United Kingdom for the same anti-competitive effects.

Lenient treatment for undertakings coming forward with information

5.32 Undertakings participating in cartel activities[35] might wish to terminate their involvement and inform the OFT of the existence of the cartel activity, but be deterred from doing so by the risk of incurring large financial penalties. To encourage such undertakings to come forward the OFT will, subject to certain conditions being met, offer total immunity from financial penalties for an infringement of Article 81 and/or the Chapter I prohibition to a participant in cartel activity who is the first to

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[34] See section 38(9) of the Act.

[35] For the purposes of the *OFT's Guidance as to the appropriate amount of a penalty* (OFT423), cartel activities are agreements which infringe Article 81 and/or the Chapter I prohibition and involve price-fixing (including resale price maintenance), bid rigging (collusive tendering), the establishment of output restrictions or quotas and/or market sharing or market dividing.

come forward. An undertaking which is not the first to come forward, or does not satisfy these conditions, may benefit from a reduction in the amount of the penalty imposed.

5.33 Further information on immunity from, or reduction in the amount of, financial penalties is set out in the *OFT's Guidance as to the appropriate amount of a penalty* (OFT423).

Leniency applications and the ECN

5.34 The European Commission and a number of NCAs also have leniency programmes that facilitate the detection of infringements[36].

5.35 As set out at paragraph 1.1 above, the Modernisation Regulation creates a system in which NCAs and the European Commission can apply Articles 81 and 82. The European Competition Network (ECN) has been set up to facilitate close co-operation between NCAs and the European Commission and to ensure an effective and consistent application of EC competition rules. An NCA will be considered well placed to deal with a case where the cumulative case allocation criteria are met. Details of these criteria are provided in the European Commission's *Notice on Co-operation with the Network of Competition Authorities* (the Notice)[37].

5.36 In most instances, where the OFT receives a leniency application (and it is well placed to deal with the case), it will remain in charge of the case. An application for leniency to the OFT will **not** be considered as an application for leniency to another authority within the ECN, even where that other authority deals with the case in parallel with or in place of the OFT. It is therefore in the interest of the applicant to apply for leniency to all the competition authorities which have the power to apply Article 81 in the territory affected by the infringement and which may be considered well placed to deal with the infringement in question. In view of the importance of timing in most existing leniency programmes,

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[36] *The Commission Notice on Immunity from Fines and Reduction of Fines in Cartel Cases* (OJ C45, 19.2.02, p 3) concerns 'secret cartels between two or more competitors aimed at fixing prices, production or sales quotas, sharing markets including bid-rigging or restricting imports or exports'. Therefore, it applies to horizontal agreements only. The OFT's civil leniency policy applies to cartel activities (see footnote 34 above), namely horizontal agreements and any form of price-fixing including resale price maintenance.

[37] Reference to be inserted

applicants will also need to consider whether it would be appropriate to make leniency applications to the relevant authorities simultaneously.

5.37 Further details on how information may be exchanged within the ECN, and the safeguards in place to protect the position of a leniency applicant with regard to such information exchange, can be found in the Notice.

Payment

5.38 Where the OFT requires an undertaking to pay a financial penalty, it must, at the same time, inform the undertaking in writing of the facts on which it bases the penalty and the reasons for requiring the undertaking to pay it[38]. Where the OFT imposes a penalty it must serve a written notice on the undertaking required to pay the penalty, specifying the date before which the penalty is required to be paid. It is likely that payment will be required within a period of three months from the date of the notice. The date for payment must not be earlier than the end of the period within which an appeal against the notice may be brought.

5.39 If the OFT finds that an undertaking is financially unable to pay the penalty by the date specified, it may (to the extent required to avoid substantially jeopardising the continued viability of the undertaking) allow payment in full by a later date or in accordance with an instalment schedule.

Enforcement of penalty decision

5.40 The OFT may require any undertaking which is a party to an agreement which has infringed Article 81 and/or the Chapter I prohibition to pay a penalty. In respect of an infringement of Article 82 and/or the Chapter II prohibition, the OFT may require the undertaking concerned to pay a penalty. Where there has been a finding of joint dominance, so that more than one undertaking has infringed Article 82 and/or the Chapter II prohibition, the OFT can require each undertaking to pay a penalty.

5.41 The term **undertaking**[39] is not defined in the EC Treaty or the Act, but its meaning has been set out in Community law. It covers any natural or legal person engaged in economic activity, regardless of its legal status

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[38] OFT's Rules, rule 8.

[39] See competition law guideline *Article 81 and the Chapter I prohibition* (OFT401).

and the way in which it is financed[40]. It includes companies, firms, businesses, partnerships, individuals operating as sole traders, agricultural cooperatives, associations of undertakings (e.g. trade associations), non-profit making organisations and (in some circumstances) public entities that offer goods or services on a given market.

5.42 A parent company and its subsidiaries will usually be treated as a single undertaking if they operate as a single economic unit, depending on the facts of each case. The OFT may need to consider the respective responsibility of both parent and subsidiary for an infringement and therefore for consequent liability to pay a penalty. Where the OFT decides to impose a penalty on both parent and subsidiary, it may be imposed jointly and severally.

5.43 A penalty may be imposed on a company that takes over the undertaking that has committed an infringement[41]. Changes in legal identity of an undertaking will not prevent it or its component parts from being penalised. As far as possible, liability for penalties will follow responsibility for actions. Thus, a subsequent transfer of a business from one economically distinct undertaking to another will not automatically absolve the transferor from responsibility. Where the original undertaking has ceased to exist by the time a penalty comes to be imposed, the penalty may be imposed on the successor undertaking.

5.44 The involvement of a trade association in an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions may result in financial penalties being imposed on the association itself, its members or both. See competition law guideline *Trade associations, professions and self-regulating bodies* (OFT408) for further details on the imposition and enforcement of financial penalties on associations of undertakings.

5.45 If an undertaking fails to pay within the date specified in the penalty notice (or such other date as may be agreed – see paragraph 5.39 above), and it has not brought an appeal against the imposition or

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[40] See case C-41/90 Höfner and Elser v Macrotron GmbH [1991] ECR 1-1979, [1993] 4 CMLR 306 and case T-319/99 Fenin v Commission (4 March 2003, unreported).
[41] See joined cases 40 to 48, 50, 54 to 56, 111, 113 and 114/73 Suiker Unie v Commission and Others [1975] ECR 1663, [1976] 1 CMLR 295.

amount of the penalty within the time allowed or such an appeal has been made and the penalty upheld, the OFT may commence proceedings to recover the required amount as a civil debt.

Appeals

5.46 The decision to impose a financial penalty and the decision as to the amount of that penalty can be appealed to the CAT by any party to the agreement in question or by the person who engaged in the conduct in question. Third parties cannot appeal decisions on penalties[42]. Such an appeal must be brought within a period specified in the CAT Rules, currently two months from the date on which the undertaking was notified of the penalty decision[43].

5.47 The CAT can impose, revoke or vary the amount of a penalty. A decision by the CAT as to the amount of a penalty can be appealed with leave to the Court of Appeal in England and Wales and in Northern Ireland, and the Court of Session in Scotland.

5.48 An appeal to the CAT against the imposition or amount of a penalty will suspend the penalty until the appeal is determined. The infringement decision itself will remain in effect (unless suspended by an interim order made by the CAT or, in the case of a further appeal, the relevant appeal court).

5.49 The CAT Rules provide that, where the CAT imposes, confirms or varies a penalty, it may in addition order that interest should be payable, as from any date after the appeal was launched, at such rate as the CAT considers appropriate. Such interest forms part of the penalty and, in the event of non-payment, is recoverable by the OFT as a civil debt in the same way as the original penalty would have been[44].

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[42] See competition law guideline *The major provisions* (OFT400).
[43] CAT Rules, rule 8.
[44] CAT Rules, rule 56(1)

6 ENFORCEMENT IN THE COURTS

Third party claims

6.1 Third parties adversely affected by an agreement or conduct which they believe infringes Article 81, Article 82, the Chapter I and/or Chapter II prohibitions may take action in the courts to stop the behaviour and/or to seek damages.

6.2 Where a decision of the OFT or the CAT (on appeal from a decision of the OFT) has already found an infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions, third parties who consider they have suffered loss as a result may bring an action for damages, against the undertaking or undertakings concerned, in the CAT or the courts. The CAT and the courts will be bound, in such proceedings, by the relevant infringement decisions, providing that the decision is no longer capable of being overturned on appeal[45].

Section 60

6.3 When applying Articles 81 and 82, the courts are bound by the case law of the European Court and by EC block exemption regulations. Section 60 of the Act provides for the United Kingdom authorities to handle cases concerned with the Chapter I and/or Chapter II prohibitions in such a way as to ensure consistency with Community law in so far as this is possible (and having regard to any relevant differences between any of the provisions concerned) and expressly refers to the decisions of the European Court and the European Commission as to the civil liability of an undertaking for harm caused by its infringement of Community law[46].

Co-operation with national courts

6.4 In any case concerning Article 81 and/or Article 82 before a court in the United Kingdom, the European Commission and the OFT each have a right to make written submissions. With the court's permission, the European Commission and the OFT may also make oral submissions to

[45] Sections 47A(9) and 58A(2) of the Act
[46] Section 60(6)(b) of the Act

the court[47]. The OFT has similar powers in respect of the Chapter I and Chapter II prohibitions.

6.5 Where a proceeding is commenced, or a defence is filed, which raises an issue relating to the application of Article 81 and/or Article 82, the party raising the issue is required to notify the OFT (in this context, not including the Regulators)[48]. This is to enable the OFT to consider whether to exercise its right to make submissions. The OFT (not including the Regulators) will notify the European Commission and/or relevant Regulators where it thinks it appropriate.

6.6 See the competition law guideline *Modernisation* (OFT442) for further details on the role of the courts.

[47] Article 15(3) of the Modernisation Regulation.
[48] Practice Direction – Competition Law – Claims relating to the Application of Articles 81 and 82 of the EC Treaty.

ANNEXE

A THE OFT'S GUIDANCE AS TO THE CIRCUMSTANCES IN WHICH IT MAY BE APPROPRIATE TO ACCEPT COMMITMENTS

Introduction

Statutory background

A.1 Section 31D(1) of the Competition Act 1998 (the Act) requires the Office of Fair Trading (the OFT)[1] to prepare and publish guidance as to the circumstances in which it may be appropriate to accept binding commitments.

A.2 EC Regulation 1/2003 (the Modernisation Regulation)[2] allows the national competition authorities of the Member States (NCAs) and the courts of the Member States to apply and enforce Articles 81 and 82 (Article 81 and Article 82 respectively)[3] of the EC Treaty[4]. The Act gives the OFT powers to enforce both the Chapter I and Chapter II prohibitions of the Act and Article 81 and Article 82. Further detail on the Modernisation

[1] Hereafter, references to the **'OFT'** in this guidance include the Regulators unless the text indicates otherwise. The **'Regulators'** are those regulators which hold powers, concurrently with the OFT, under Part I of the Act.

[2] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (OJ L1, 4.1.03, p 1).

[3] **Article 81** prohibits agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market. **Article 82** prohibits conduct by one or more undertakings which amounts to an abuse of a dominant position within the common market or a substantial part of it in so far as it may affect trade between Member States. **The Chapter I prohibition** and **the Chapter II prohibition** of the Act are based on Article 81 and Article 82 respectively but apply to anti-competitive practices which affect trade within the United Kingdom. For further details see the competition law guidelines *The major provisions* (OFT400), *Article 81 and the Chapter I prohibition* (OFT401) and *Article 82 and the Chapter II prohibition* (OFT402).

[4] The Treaty of Rome, establishing the European Community, as consolidated by the Treaty of Amsterdam.

Regulation is set out in the competition law guideline *Modernisation* (OFT442).

A.3 Under section 31A(2) of the Act the OFT may, instead of continuing with an investigation into an alleged infringement of Article 81, Article 82, the Chapter I and/or Chapter II prohibitions of the Act, and for the purposes of addressing the competition concerns it has identified, accept such binding commitments offered to it by a person or persons as it considers appropriate.

A.4 Under section 31A(3) of the Act, where the OFT has accepted binding commitments it may, for the purposes of addressing the competition concerns which it identified at the time of such acceptance or for the purposes of addressing any new competition concerns it has identified, accept from the person or persons who gave the commitments a variation of them or commitments in substitution for them.

A.5 Under section 31A(4)(b) of the Act, the OFT may release binding commitments.

A.6 By virtue of section 31D(8) of the Act, the OFT must have regard to the guidance for the time being in force when considering whether to accept any commitments offered to it. Although there is no statutory obligation on the Regulators to publish guidance as to the circumstances in which it may be appropriate to accept binding commitments, the Regulators are required to have regard to the guidance for the time being in force when considering whether to accept any commitments offered to them.

A.7 This guidance was approved by the Secretary of State as required under section 31D(4) of the Act on [date to be inserted].

A.8 Section 31D(2) of the Act provides that the OFT (not including the Regulators) may alter the guidance on commitments at any time. Any such alterations must be made with the approval of the Secretary of State and following consultation with such persons as the OFT (not including the Regulators) considers appropriate.

A.9 This guidance on commitments will be reviewed in the light of experience in applying it over time.

Policy objective

A.10 This guidance has been drafted to increase transparency by setting out the circumstances in which the OFT may consider it appropriate to accept binding commitments and the circumstances in which the OFT will not consider it appropriate to accept binding commitments. It is intended that this guidance should be of assistance not only to those who are parties to an agreement[5] or conduct, but also to their customers and other businesses.

Circumstances in which it may be appropriate to accept commitments

A.11 The decision whether to accept binding commitments is at the discretion of the OFT.

A.12 The OFT is likely to consider it appropriate to accept binding commitments only in cases where:

- the competition concerns are readily identifiable
- the competition concerns are fully addressed by the commitments offered, and
- the proposed commitments are capable of being implemented effectively and, if necessary, within a short period of time.

A.13 The OFT will not, other than in very exceptional circumstances,[6] accept binding commitments in cases involving secret cartels between competitors which include:

- price-fixing
- bid-rigging (collusive tendering)
- establishing output restrictions or quotas
- sharing markets, and/or
- dividing markets.

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[5] 'Agreement' here includes decisions by associations of undertakings and concerted practices.
[6] For example cases which might feature the restrictions listed in paragraph A.13 but where the OFT considers that the administrative cost involved in continuing the investigation and proceeding to a final decision would outweigh the benefits.

Nor will the OFT accept binding commitments in cases involving serious abuse of a dominant position[7].

A.14 The OFT will not accept binding commitments in circumstances:

- where compliance with and the effectiveness of any binding commitments would be difficult to discern, and/or
- where the OFT considers that not to complete its investigation and make a decision would undermine deterrence.

A.15 Binding commitments will generally be adopted for a specified period of time. They are treated as released on the expiry of this period.

A.16 Whilst binding commitments are in force, the OFT may review their effectiveness and take such action as regards variation or release as it deems appropriate.

A.17 If different competition concerns are identified by the OFT, the appropriateness of accepting varied or substitute commitments will take into account the considerations in paragraphs A.12 to A.14 above.

A.18 Once binding commitments have been accepted in respect of an agreement or conduct, the OFT may not make an infringement decision in respect of that agreement or conduct unless it has:

- reasonable grounds for believing that there has been a material change of circumstances since the commitments were accepted
- reasonable grounds for suspecting that a person has failed to adhere to one or more of the terms of the binding commitments, or
- reasonable grounds for suspecting that information which led it to accept the binding commitments was incomplete, false or misleading in a material particular.

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[7] It is the OFT' s assessment of the seriousness of an abuse and its effect on competition which will be taken into account in determining whether commitments are appropriate in a particular case. When making its assessment, the OFT will consider a number of factors, including the nature of the product, the structure of the market, the market share(s) of the undertaking(s) involved, entry conditions and the effect on competitors and third parties. The damage caused to consumers whether directly or indirectly will also be an important consideration. This assessment will be made on a case by case basis, taking account of all the circumstances of the case. However, as a general rule, the OFT will regard predatory pricing as a serious abuse.

A.19 However, the OFT is not prevented from taking action in relation to competition concerns other than those addressed by the commitments it has accepted.