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14 June 2011

Department for Business Innovation and Skills
3rd Floor, Orchard 2
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Dear Sirs

**A Competition Regime for Growth: ORR response to the consultation on options for reform**

We welcome this opportunity to participate in your review of the competition regime. Although the UK competition regime is highly regarded internationally it needs continually to improve, to respond to the needs of the economy and to give businesses the confidence they need to grow and make investment and employment decisions without uncertainty arising from lengthy investigations and unnecessary scrutiny.

We welcome moves, therefore, to make competition powers easier to use and to simplify processes. There is a tremendous opportunity here to learn from experience; to take the best of the current system including improvements already implemented and to introduce change particularly to address residual criticisms around unfairness and burden.

We believe that sector regulators can bring significant expertise and experience to the design of a new framework. Importantly sector regulators share the objective of making markets work in the interests of consumers and will use the most appropriate tools at their disposal to make this happen.

*The importance of competition concurrency for the regulatory framework*

The Office of Rail Regulation (ORR) is the independent safety and economic regulator for Britain's railways. The ORR is led by a Board, appointed by the Secretary of State for Transport.

One of our key strategic objectives is that "*Passengers and freight customers benefit fully from improved safety, performance, efficiency and capacity*"[1]. Our approach for achieving this is to promote, where possible, effective market mechanisms and competition, because these are more likely to be responsive to the changing needs of rail users and more likely to lead to better outcomes than regulatory mechanisms alone[2]. Where market mechanisms fail, economic, competition and consumer policy all play their part in the design of the most appropriate framework for intervention.

The consultation document makes an important point[3] that the removal of concurrency may actually impede that integrated application of powers and reduce the scope to apply the sector regulator's industry expertise to competition. It is also true that clarity about what competitive outcomes could lead to can help to shape regulatory regimes in a way which leaves regulated markets more open to competition, even where there are constraints on how far it is sensible to use competition powers as the primary instrument to achieve better outcomes for consumers.

**For this reason we welcome the recommendation - and believe that it is very important - that sector regulators should maintain their concurrent antitrust and market investigation reference powers** (and looking forward to the upcoming consultation on the reform of the consumer landscape, we welcome too the emerging view that sector regulators retain consumer enforcement powers in the new structure[4]). The continued interaction with the regulated sector over time gives the regulatory authority the knowledge and empirical evidence it needs to respond appropriately. It also provides the sector with the confidence it needs that economic regulation will be rolled back in full understanding of the implications and that it has a regulator who can react swiftly where there is evidence of harm.

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[1] Theme 1, *Promoting safety and value in Britain's railways*, *ORR's strategy for 2009-14*

[2] Paragraph 9, ibid

[3] Paragraph 7.15

[4] Paragraph 9.21 of the consultation

Our preference, as a regulator, is to use competition tools wherever possible. Our track record attests to this. We have undertaken eleven investigations over the past ten years, one of which resulted in an infringement decision and associated penalty of £4.1m. We believe that this decision had a reputational impact beyond the decision alone and contributed significantly to the subsequent liberalisation of the railfreight market. We also, in 2007, referred the passenger rolling stock market to the Competition Commission (CC) using our market investigation reference powers. To remove concurrency we believe would send out the wrong signals to the sector.

We also consider ourselves to have close working relationships with the CC and the Office of Fair Trading (OFT) and have welcomed discussions on issues of policy and procedure with both bodies. We have additionally on two previous occasions seconded an OFT officer to assist on on-site inspection and this worked very well from our perspective.

The concern among critics that there is a paucity of cases in the regulated sectors and that this results from the UK's system of concurrency, seems not to be supported by the evidence. We note, for example, that the proportion of railway cases amongst competition authorities in member states where concurrency does not exist are a very small proportion of the total cases investigated[5]. This is more likely to reflect the nature of rail markets and the application of prioritisation criteria than the favouring of sector specific legislation, as is the criticism here.

However, we regulate in a sector where passenger train services are provided under franchises which are specified, competitively tendered, let, monitored and enforced by government and where regulation continues to play a critical role in the delivery of tax-payer funded outputs.

The recent rail value for money study[6] has recommended a move towards a more conventional regulatory model in the sector, with a bigger role for independent regulation of train operators, and we are considering with the Department for Transport whether and how this could be implemented. Importantly, the report also set out recommendations for improved efficiency and value for money in the rail industry and highlighted the challenge facing the whole rail industry if the recommended target of £1bn per year of savings is to be achieved. It is likely to lead to a period of change in the industry and its regulation.

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[5] For example since 2000 the number of railway cases compared to total cases investigated in the four member states that we hold statistics for were as follows: in the Czech Republic one out of 220; in Spain seven out of 692; in Finland three out of 4902; and in France seven out of 639. Since 2007 in Belgium there have been 0 cases out of a total of 53.

[6] *Realising the Potential for GB Rai*l – Report of the Rail Value for Money Study, May 2011

Regulation will, for the time being at least, continue to have a role in the railways not least in helping to create the ground rules for a more cohesive railway in which all parties co-operate for the purpose of delivering the high quality, efficiently priced railway which taxpayers; passengers and users of rail-freight services are looking for as demand continues to grow.

**The removal of concurrency or the proposed alternative[7] of providing the CMA with the power to question each regulatory decision; each regulatory approach; and to direct the form of regulatory intervention are entirely inconsistent with commitments provided by government as to the importance of independent regulation in providing the predictable and stable framework that business needs to invest[8].**

This is particularly concerning in a sector where there is a requirement for significant investment to accommodate growth in demand and to meet the needs of users and of the economy as a whole. Total public and private sector spending on the railways currently amounts to about £11bn per year. In recent years, much rail investment has relied on government guarantees. Government and ORR believe it is important for the private sector to play a bigger role in financing investment and to take more risk. A stable and predictable regulatory regime, reflecting the needs of the sector, will be a key enabler for this.

Similar concerns exist around the proposal that the CMA be provided with an objective or duty to keep key sectors under review. Although we understand that there can be benefits from reviews being undertaken, from time to time, by a 'fresh pair of eyes' there are also countervailing risks of dampening progress and innovation in sectors which are already under a significant amount of scrutiny.

*The relationship with the CMA going forward*

We value challenge, however, and believe that it leads to better and more rigorous decision making. We understand also that there is a need for an authority with overall responsibility for setting the strategy for competition policy and for ensuring that those who operate concurrently are cognisant of and are moving in the same direction of travel. However, the speed of travel will inevitably reflect the nature and characteristics of the

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[7] Paragraphs 7.30-7.32

[8] Commitment 2 in which the Government acknowledges the need not to erode the independence of regulation over time and commits to amongst other things to: "[…] *preserve the independence of economic regulators. […] ensure that: regulators' staff and management act independently from any market interest and do not seek or take direct instructions from any government or other public or private entity when making regulatory decisions.*

sector involved. **We would be happy to have closer bi-lateral engagement with the CMA in the future which recognises the competition policy lead on the one hand and the sector specific expertise on the other.**

There are also undoubtedly major benefits in the CMA becoming a centre for expertise in competition policy and enforcement. As noted above we already have experience of asking the OFT and CC for advice and assistance and, from our perspective, this has worked very well. We look forward to developing options which enable such joint working in the future.

*Regulatory appeals*

We note that the preferred option here is to essentially 'lift and shift' appeals currently heard at the CC to the newly merged CMA and there are various options in terms of how such appeals will be heard in the new structure, although these are not fully developed in the consultation. Our major concerns going forward around appeals – and we are happy to work through the detail of this as the proposals develop – are:

- that the panel appointed to hear such appeals is sufficiently separate so as not to appear biased by association with concurrent relationships (which is a concern with the preferred option); and of course

- that the panel has sufficient expertise to hear cases which given their statutory genesis will require understanding of a broad range of disciplines.

We are also happy to be part of an initiative for regulators to develop model regulatory processes for adoption over time but the challenge will be considerable given the significant differences in statutory frameworks.

**Summary**

We are ready to play a full part in developing a framework which delivers the objectives of the reform and enables close and mutually beneficial working relationships between the CMA and regulators. The challenge will be to create a framework which allows each regulated sector to move from a world of regulatory rules and processes to one which relies much more on competition case law and precedent at a speed which suits its own evolutionary progress. The objective must be to avoid unnecessary uncertainty and risk to industry; and importantly delayed remedy for the consumer and the tax-payer during the period of design and in implementation.

There is a significant body of work wrapped up within the proposals and a period of transformation which will require us all to contribute so as to bring about the improvements we all want, without losing what is excellent about the current system in the process.

Yours faithfully

BIS | Department for Business Innovation & Skills

# A competition regime for growth: a consultation on options for reform.

## Response form

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Please tick one box from a list of options that best describes you as a respondent. This will enable views to be presented by group type.

| | |
|---|---|
| | Small to Medium Enterprise |
| | Representative Organisation |
| | Trade Union |
| | Interest Group |
| | Large Enterprise |
| | Local Government |
| | Central Government |
| | Legal |
| | Academic |
| ✓ | Other (please describe): Regulator |

**When responding please state whether you are responding as an individual or representing the views of an organisation. If responding on behalf of an organisation, please make it clear who the organisation represents and, where applicable, how the views of members were assembled.**

**This response represents the views of ORR.**

## Consultation Questions

*Why reform the competition regime?*

This chapter sets out an assessment of the strengths and weaknesses of the UK competition regime and proposes to reform it to: improve the robustness of decisions and strengthen the regime; support the competition authorities in taking forward the right cases; and improve speed and predictability for business.

***Q.1** The Government seeks your views on the objectives for reform of the UK's competition framework, in particular:*

- *improving the robustness of decisions and strengthening the regime;*
- *supporting the competition authorities in taking forward the right cases;*
- *improving speed and predictability for business.*

***Q.2** The Government seeks your views on the potential creation of a single Competition and Markets Authority.*

Comments: [Chapter 1 – Why reform the competition regime?]

There is a significant body of work wrapped up within the proposals and an inevitable period of transformation which will require careful management to deliver the sought for improvements without losing what is excellent about the current system in the process.

A particular concern must surely be the possibility that such a major change embracing both structure and process could result in a regrettable diminution in the service provided currently and an ensuing loss of credibility in the system and loss to the consumer at a time when we are facing severe challenges for the economy.

There will be an inevitable resource consequence to the development of the proposals and the implementation of change and although we want to work with BIS to follow through on some of the detail of the proposals, this is also a significant period of change in the railways (see covering letter). It would undoubtedly be easier to advise and contribute to the latter with greater certainty about what the competition framework will look like going forward and what our role will be within it.

In summary we wonder whether it would be more sensible to adopt a more stepped approach to change.

That said we remain supportive of options which increase speed; efficiency; and certainty. And it can only be a good move to reduce burdens on both regulators and industry, whilst at the same time retaining the integrity of the current system. We believe there are some good ideas which are worthy of development around decreasing overlaps in the two phase market investigation regime and introducing more rigour in timescales in both this and in anti-trust investigations including ensuring that opportunities for game-playing are avoided. This is also an opportunity to address concerns around confirmation bias and/or unfairness.

We also see major benefits in the CMA becoming a centre for expertise upon which regulators can draw (particularly where greater reliance on competition rather than ex-ante intervention is likely to lead us into unchartered waters in terms of precedent and will start to test the boundaries of current thinking particularly on exploitative abuse of dominance cases). Though this will need to be carefully managed so as not to erode and ultimately undermine regulatory independence.

In terms of the detail there needs to be more clarity around how sector regulators will interact and fit within the governance arrangements and decision making in the new structure (for example, proposals in chapter 10 around closer interaction between phase 1 and phase 2 staff to minimise overlap in market investigations; in chapter 5 questions around where sector regulator cases will be adjudicated; and in chapter 8 the future of licence and price determination appeals).

*The UK Competition regime and the European context*

This chapter sets out the UK institutions that make up the competition regime and their functions, as well as the European context.

Comments: [Chapter 2: The UK Competition regime and the European context]

It is critical to an understanding of how competition law applies in the rail sector to appreciate that certain of our principal economic functions cover territory that would in an unregulated sector usually fall to be governed by competition law. Furthermore and relevant to this section of the consultation, railway sector specific regulatory scrutiny and intervention is also increasingly driven by requirements in European legislation.

For example,

The **First Railway Package**, which was adopted by the European Commission in 2001, includes measures to:

- open the international rail freight market;
- clarify the formal relationship between the State and the infrastructure manager and between the infrastructure manager and train operators; and
- introduce a defined policy for capacity allocation and infrastructure charging.

The **Second Railway Package** was adopted by the European Commission in 2004. Its aim is to create a legally and technically integrated European railway area. It includes Directives that:

- harmonise and clarify interoperability requirements;
- open up both national and international freight services on the entire European network from 1 January 2007; and
- set up a steering body, the European Railway Agency, to co-ordinate groups of technical experts seeking common solutions on safety and interoperability.

The **Third Railway Package**, which was adopted by the European Commission on 26 September 2007, is designed to open up international passenger services to competition within the EU by 2010. It includes measures to:

- deal with the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure. It envisages opening the market for international passenger services to competition from 1 January 2010;
- establish the conditions and procedures for the certification of train crews operating

locomotives and trains across Europe; and

- establish rail passengers' rights and obligations around, for example, insurance, compensation and ticketing.

Other relevant European legislation include:

- Regulation (EC) No 1370/2007 of the European Parliament and of the Council of 23 October 2007 on public passenger transport services by rail and by road.
- Communication from the Commission — Community guidelines on State aid for railway undertakings.
- Regulation (EU) No 913/2010 of the European Parliament and of the Council of 22 September 2010 concerning a European rail network for competitive freight.

Article 30 of Directive 2001/14/EC requires Member States to appoint an independent regulatory body, as a charging body, an allocation body and a body to whom applicants may lodge an appeal if they feel unfairly treated, discriminated against or in any other way aggrieved.

Regulation 30 of The Railways Infrastructure (Access and Management) Regulations 2005 (which transpose and implement a number of the requirements of the First and Third Package and which came into force on 28 November 2005) establishes ORR as that regulatory body and provides us with the three interlinking roles of:

- monitoring competition;
- dealing with complaints from aggrieved parties; and
- whether on our own initiative, or as a result of a complaint, taking appropriate measures to correct undesirable developments.

The measures contained in the three packages in essence accept that competition policy alone is not sufficient to deliver the objective of fully liberalised and competitive railway markets operating freely across member states.

Although we exercise our responsibilities as a national regulatory body '*without prejudice'* to Community and national regulations concerning competition policy[9], the interplay between the two areas is complicated. The design of a domestic competition framework needs to have cognisance of this not least because it facilitates understanding of the current scope for some of the proposals to deliver their objective of increased reliance on

[9] EU Directive 91/440, Article 5 point 7

competition tools alone.

In common with Slovakia, the Netherlands and Macedonia we are both the national regulatory body and competition authority for the railways.

*A stronger markets regime*

This chapter sets out that there is scope to streamline processes and make the markets regime more vigorous. The key options are: enabling in-depth investigations into practices that cut across markets; giving the CMA powers to report on public interest issues; extending the super-complaint system to SME bodies; reducing timescales; strengthening information gathering powers; simplification of review of remedies process; and updating remedial powers.

***Q.3** The Government seeks your views on the proposals set out in this Chapter for strengthening the markets regime, in particular:*

- *the arguments for and against the options;*
- *the costs and benefits of the options, supported by evidence wherever possible.*

***Q.4** The Government also welcomes further ideas, in particular, on modernising and streamlining the markets regime, and on increasing certainty and reducing burdens.*

Comments: [Chapter 3 – A stronger markets regime]

We are pleased that BIS is proposing to retain the two stage process for market investigations. We consider there to be significant value to having access to a 'fresh pair of eyes' and this was certainly a consideration for ORR when we referred the **market for the leasing of passenger rolling stock to the CC in 2007**. We noted in our findings that these markets had been scrutinised to a greater or lesser extent on a number of previous occasions: by the Office of the Rail Regulator in 1998, (following a request from the Deputy Prime Minister); by the Strategic Rail Authority as part of its rolling stock strategy in 2003; and by the Secretary of State as part of his review, *The Future of Rail* (published in July 2004). We thought it important that an authority with no previous history in this area should provide the means for an in-depth independent review, in order to, amongst other things, give greater credibility to the findings.

We do, however, agree that the two phase system can create overlap and that the new framework should look to address this. We support, for example, the proposal to provide investigatory powers for the first stage (and ask for this to be extended to sector regulators). In our view this would provide two key advantages in that it is likely to:

- help to speed up the first phase. Our own experience is that there are challenges in asking for information voluntarily both in terms of what you can reasonably ask for and the extent to which you can push timescales; and

- be capable of providing a body of evidence which since given under legal direction is more likely to be able to be relied upon in the second stage.

We are also supportive of moves to tighten up on timescales.

As a first stage authority we have structured our framework for market monitoring[10] (see below) to keep the burden to industry proportionate to the stage that we have reached (for example, our 12 week 'diagnostic stage' which is designed to assess the existence, potential scale and impact of any problems mainly relies on information and data already available to us and relies only infrequently on interviews with third parties). We are also mindful of the possibility that a second stage investigation (our public study – which is nearest in equivalent to the OFT Phase I study) could lead to a reference. We, therefore, aim to complete such a study within six months.

Based on our experience, it is possible that more cases could be referred from regulated sectors if there was a way to fashion timescales to suit the scale of the problem.

[10] ORR's approach to reviewing markets, October 2009: http://www.rail-reg.gov.uk/upload/pdf/407.pdf

The principles of good regulation demand that regulation should not impose costs to business which are disproportionate and outweigh the (potential) value of the benefits achieved. The factors (set out in our guidance referred to above) that we will take into account in exercising our discretion to refer include:

- the nature and significance of the competition problems that we believe exist in the market concerned; and
- whether a reference would be a proportionate response to the scale of the competition problems identified.

At paragraphs 131-132 of *ORR's consultation on the findings of its Rail freight sites public study*, May 2011 we set out how these factors affected our decision on whether or not to refer this market to the CC. Our findings here are currently out for consultation with responses due back on 29 July. It is possible that the responses will be enlightening in the context of the review of the competition framework.

In this context there may be merit in pursing the idea of providing the CMA with powers to carry out 'horizontal' investigations (3.9 of the consultation) for features or practices that affect more than one market. Although the scope and scale of such investigations should not be underestimated and there would need to be significant co-operation between regulated sectors and the CMA to ensure that such reviews were properly resourced and informed.

There needs to be some more clarity about how some of the proposals are expected to be extended to sector regulators i.e. proposals around statutory definitions and thresholds (particularly proposals which could limit our discretion on how we discharge our various responsibilities to monitor markets[11]) and the proposal at paragraph 10.33 that "*some or all of the phase 1 market study team would continue work on the phase 2 investigation, taking with them their existing knowledge of the case and market*."

We set out at the end here some key elements of ORR's market studies framework in

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[11] Specifying in a high degree of detail the manner in which a regulator is to achieve its objectives limits the scope of the regulator to identify or achieve the optimal outcome because those tools and inputs form, in effect, objectives in their own right. Specifying tools and inputs may also undermine the benefits associated with independent economic regulation. For these reasons, regulators' duties should be outcome-focused and avoid specifying means, tools or inputs." (paragraph 39 of BIS principles of economic regulation)

[12] Section 82 of the Railways Act defines railway services as: services for carriage of passengers, carriage of goods by railway, light maintenance services, station services and network services.

[13] Article 30 (2001/14/EC) requires Member States to appoint a regulatory body, independent of the Infrastructure Manager, as a charging body, an allocation body and to whom applicants may lodge an appeal if they feel unfairly treated, discriminated against or in any other way aggrieved.

order to facilitate understanding of the statutory background; our approach and the different terms that we use.

We are not particularly supportive of the proposal at 3.39-40 to revise the duty to consult on decisions not to refer. We are committed to transparency and accountability and consider that this is an important part of making good decisions and ensuring that all views and evidence have been captured in our final conclusions.

Finally we note the proposal to amend Schedule 8 of EA02 to require parties to publish non-price information and agree that information remedies can be an effective solution to lack of competition in some markets. However, in this context we draw attention to *Realising the Potential of GB Rail, Report of the Rail Value for Money Study, Summary Report,* published May 2011 which states at paragraph 6.11:

"…*the Study is aware of the remedies put forward by the Competition Commission following its review of the rolling stock leasing market. However, although it is too early to make a full assessment of the effect of those remedies, the Study finds it difficult to understand how these remedies will give the DfT sufficient information to satisfy itself that rates on re-leases are value for money*…"

The thoughts of the author might be helpful in delivering further improvements to the system.

ORR's approach to reviewing markets

The legal framework for our market monitoring responsibilities comes from:

- **Section 69 of the Railways Act 1993** - this provides that we must, so far as it appears practicable from time to time, keep under review the provision of "railway services"[12] in Great Britain and elsewhere. We must also (again so far as it appears practicable from time to time) collect information, with respect to the provision of those services, in order to facilitate the exercise of our functions under Part 1 of the Railways Act 1993;

- **Article 10(7) of Directive 2001/12** on the development of the Community's railways, was implemented in Great Britain by the Railways Infrastructure (Access and Management) Regulations 2005. These require the regulatory body established under Directive 2001/14[13] (i.e. ORR in Great Britain) to monitor competition in rail services markets and on the basis of a complaint; and

- As a concurrent competition authority under **the Enterprise Act.**

Two points:

- concurrent jurisdiction under the Enterprise Act and the Competition Act goes wider than the definition of railway services in section 82 of the Railways Act and includes services such as the leasing or maintenance of rolling stock as provided by the rolling stock companies (ROSCOs), the supply of goods and services to Network Rail, and the provision and purchase of goods and services to, or by, London Underground Limited (LUL); and

- we are also the competition authority and regulatory body for the Channel Tunnel Rail Link (CTRL). Our jurisdiction as a regulatory body does not extend to the tunnel or to shuttle services. However, allocation of competition cases involving the tunnel and international railway services travelling through the UK from Europe would be a matter decided between the relevant national competition authorities including ORR.

Our approach to market scrutiny consists of thee potential stages:

- an initial **diagnostic research study** (usually lasting up to three months) in which we will gather information in-house: from our own records; governmental; and public sources, in order to assess how a market is functioning and whether there appear to be market problems that warrant further attention.

- a more detailed consultative **public study** (usually lasting up to six months), including consultation with external stakeholders, in which we make a fuller assessment of any concerns identified during the research study.

- a concluding **remedies study** (usually lasting up to twelve months), including further engagement and appropriate public consultation with external stakeholders in which we reach a view on the appropriate remedies for market problems, we would use this stage, for example, to develop undertakings in lieu of a market investigation reference.

A reference to the CC is most likely to result from a public study and in our published terms of reference for a public study we will identify a reference as a possible outcome. A public study is the closest equivalent to a Phase I study. We undertake approximately two-four diagnostic studies per year (depending on size). Last year 2010-11, this resulted in one public study.

*A stronger mergers regime*

This chapter sets out that there is scope for improving the merger regime by addressing the disadvantages of the current voluntary notification regime and streamlining the process. The Government is seeking views on: (1) options to address the disadvantages

of the current voluntary notification regime; (2) measures to streamline the regime by reducing timescales and strengthening information gathering powers; (3) introduction of an exemption from merger control for transactions involving small businesses under either a mandatory or voluntary notification regime. We ask:

***Q.5** The Government seeks your views on the proposals set out in this Chapter for strengthening the mergers regime, in particular:*

- *the arguments for and against the options;*
- *the costs and benefits of the options, supported by evidence wherever possible.*

***Q.6** The Government seeks views on which approach to notification would best tackle the disadvantages of the current voluntary regime?*

***Q.7** The Government welcomes further ideas on streamlining the mergers regime.*

Comments: Chapter 4- A stronger Merger regime

No comments here.

*A stronger antitrust regime*

This chapter sets out three options for achieving a greater throughput of antitrust cases: (1) retain and enhance the OFT's existing procedures; (2) develop a new administrative approach; (3) develop a prosecutorial approach. We also ask about the case for statutory deadlines for cases and for civil penalties for non-compliance with investigations, set out considerations relating to private actions and invite views on the powers of entry and of investigation and enforcement.

***Q.8** The Government seeks your views on the proposals set out in this chapter for strengthening the antitrust regime, in particular:*

- *Options 1-3 for improving the process of antitrust enforcement;*
- *the costs and benefits of the options, supported by evidence wherever possible.*

***Q.9** The Government also seeks views on additional changes to antitrust and investigative and enforcement powers in paragraphs 5.48 to 5.57, and the costs and benefits of these.*

***Q.10** The Government welcomes further ideas to improve the process of antitrust investigation and enforcement.*

Comments: [Chapter 5 – A stronger Antitrust Regime]

Anti-trust

The key issues to be addressed here appear to be:

- timescales (the need to reduce the burden on business and to increase certainty and to incentivise the throughput of more cases); and
- perceived procedural unfairness and bias.

Timescales

We support moves to insert more certainty and efficiency into the system and consider

that there are considerable efficiencies to be gained already from improvements put in place recently by the OFT. In particular we consider the establishment of a **Procedural Adjudicator** to be an excellent move and if it proves successful should be maintained within the new system – open also to the sector regulators to use. Our experience on the long running EWS case (identified at table 3 of Appendix 2 to the consultation) was that procedural dispute featured very heavily from outset. Parties need, however, to be bound by the Adjudicator's decision and there needs to be a presumption that the Adjudicator is used in preference to the Courts.

Similarly we are supportive of proposals to create offences under CA98 and EA02 for non-compliance with an investigation (paragraph 5.53 of the consultation). We agree that pursuing a criminal prosecution for non-compliance in most cases would not appear to be the most proportionate or appropriate measure to take. Non-compliance takes various forms and is rarely an all out rejection of the authority of the investigator and is more to do with pushing the boundaries of reasonableness on timescales for responding; creating difficulties around the retrieval of information and data; and responding to the letter not the spirit of the requests. All of these exchanges create drag and difficulties in keeping to timescales and the scope for game playing is huge. We agree with the view at paragraph 5.55 of the consultation that the ability to propose fines similar to those available to the Competition Commission currently would incentivise parties in a positive direction.

At ORR we have introduced targets within our procedures to reach a non-infringement decision or a statement of objections (SO) within six months of opening the case. Our thinking is that the statement of objections will set out the case on the basis of the evidence gathered to date and there is a chance that it may not, at that stage, be resilient to challenge. A decision would then be made whether there was sufficient evidence to move to a further SO (which addresses the response and moves the case forward) or to close the case by way of a non-infringement decision. Those timescales would not withstand the rigour of then having to argue our case before another authority. The SO would in effect become the de facto decision and the timescales could extend accordingly. We are, therefore, concerned at proposals which would require the sector regulator or first phase investigator at the CMA to argue the case before a Tribunal at this stage (either in the Administrative or Prosecutorial model) and seriously doubt that it would deliver the reduction in timescales that this proposal is seeking to achieve.

<u>Bias</u>

We note here options around establishing a system whereby investigation is separated from adjudication. Our key concerns around these proposals are:

- how sector regulators would fit into this framework which is predominately drafted around how the newly merged CMA would work;
- and concerns about timescales if the SO effectively became the de-facto decision (see above).

How ORR currently deals with cases

Our current practice is to brief but not to involve the senior team or the Board in the conduct of an investigation. This is to:

- reduce confirmation bias from any final decision; and
- discourage lobbying of the senior team which might otherwise occur given the dual relationship that we have with the industry as sector regulator and to ensure focus on the facts and substance of the case.

Hearings are chaired by a director separate to the investigatory team.

At SO stage a Committee of the Board is established with the dual function of:

- challenging the team; and
- providing assurance to the Board that all issues have been covered.

A Decision is a matter reserved to the Board.

To reduce even further the possibility of confirmation bias we could consider delegating the decision on whether to move to an SO to the Chief Executive.

A further option (and one not discussed within Chapter 5 where the focus is on how the system would work within the CMA) is for regulators to establish an impartial and independent panel system for the hearing of such cases, either independently or jointly. Issues for consideration here are, however:

- the panel would need to be seen to be sufficiently separate and impartial and in an organisation the size of ORR that would probably mean the establishment of a call-off specialist panel – called in to make decisions only when required; and
- the implications of establishing different processes for making decisions on competition matters and those made in the course of our sector specific role.

The two stage variant at 5.39 is not addressed in any detail here and is the least persuasive of the options. It does not address the issue of confirmation bias and would create a bottle neck of cases presented all at reasonable suspicion stage. We would be concerned if any application of prioritisation criteria resulted in a sector case being closed due to resourcing implications at the time.

In summary it is important that any new system retains the benefits of:

- non-infringement decisions fully argued and capable of setting rules for future behaviour;

- fully argued decisions where the underpinning economics are fully set out and thus capable of providing guidance in an effects based regime; and

- the ability to settle.

In relation to the second bullet we have concerns around moving toward a system where appeals dealt with on the same basis and grounds as those made to the European General Court against decisions of the European Commission. We ask whether this would provide the richness of economic discussion which has become a feature of appeals on the merits at the CAT. This is particularly important if we are to move to a world where ex-ante rules no longer form a part of the regulatory framework.

Such an approach may increase the volume of cases and make the UK throughput more comparable with that of competition authorities in other member states (as set out at Table 5.1) but the cases themselves may not be as capable of moving competition policy forward beyond the existing per se application of the law.

*The criminal cartel offence*

This chapter sets out options for making the cartel offence easier to prosecute: (1) removing the dishonesty element and introducing prosecutorial guidance; (2) removing the 'dishonesty' element and defining the offence so that it does not include a set of 'white listed' agreements; (3) replacing the 'dishonesty' element of the offence with a 'secrecy' element; (4) removing the 'dishonesty' element and defining the offence so that it does not include agreements made openly.

***Q.11** The Government seeks your views on the proposals set out in this Chapter to improve the criminal cartel offence, in particular:*

- *the arguments for and against the options;*
- *the costs and benefits of the options, supported by evidence wherever possible.*

***Q.12** Do you agree that the 'dishonesty' element of the criminal cartel offence should be removed?*

***Q.13** The Government welcomes further ideas to improve the criminal cartel offence.*

Comments: [Chapter 6 – The criminal cartel offence]

No comments here.

*Concurrency and sector regulators*

This chapter sets out three options for improving the use and coordination of competition powers: (1) sector regulators could agree on a common set of factors to take into account when deciding whether to use sectoral or competition powers or competition law primacy could be enhanced; (2) the CMA could act as a central resource for the sector regulators; (3) the CMA could coordinate the use of competition powers across the landscape.

***Q.14** Do you agree that the sector regulators should maintain their concurrent antitrust and MIR powers in parallel to the CMA?*

***Q.15** The Government also seeks views on the proposals set out in this Chapter for improving the use and coordination of concurrent competition powers in particular:*

- *the arguments for and against the options;*
- *the costs and benefits of the options, supported by evidence wherever possible.*

***Q.16** The Government welcomes further ideas to improve the use and coordination of concurrent competition powers.*

Comments: [Chapter 7 – Concurrency and the sector regulators]

We have set out our commitment to and case for concurrency in the covering letter and the risks of withdrawal in particular:

- Concurrency and the knowledge that it brings is an integral part of our regulatory approach. It moreover provides us with the credibility to advise government on railway policy and the implications of railway structural and franchise reform. It provides us with the opportunity to promote competition as an important stimulus of economic growth.

- Our competition resource is not confined to the pursuit of cases but is called upon in the development of regulatory policy. Similarly our knowledge of the sector provides significant efficiencies to us in the investigation of cases. Our recent non-infringement decision involving the carriage of petrochemicals by rail was completed within six months, a timescale made possible by our sector understanding of industry costs. We would caution against moving toward a system which seems to promote policy silos and where the direct interaction between economic regulation and competition policy will be lost.

- We support the case for rolling back regulation in line with increased competition but to do so needs an understanding of the implications. Removing concurrency could lead to regulators being even less inclined to rely on ex-post intervention, if that is then outside of their control and expertise. Removing concurrency would send out the wrong signals to the regulated sectors.

- Further, there is no compelling argument that ending concurrency will lead to more cases. On the contrary the inevitable resource constraints on a single body could mean that railway cases (which are sometimes small in value; limited to Article 102 (abuse of dominance cases rather than cartels); and perhaps of less relevance to the economy as a whole than abuses taking place in other sectors) might not be prioritised. See comparative data from other member states set out in the covering letter.

We have also set out in our response to Chapter 2 (which covers the vast range of European legislation that covers this sector) how it is critical to an understanding of how competition law applies in the rail sector to appreciate that certain of our principal economic functions cover territory that would in an unregulated sector usually fall to be governed by competition law. For example we,

- determine through periodic reviews Network Rail's outputs and funding, reflecting government specifications and the money available and set charges which train operators pay for access to the track. We monitor and enforce delivery of those outputs through Network Rail's licence; and

- approve or, where terms are not agreed between the parties, direct the terms by which access is granted to train operators to use track, stations and light

maintenance depots. Under European legislation we have an appeal role for a broader range of railway facilities than are covered by domestic legislation.

This should set in context:

- the volume of cases (both non-infringement and infringement decisions which we have made); and
- the extent to which more cases will result from implementation of the proposals outlined in the consultation.

Further elements of the railways regulatory structure which are relevant here are:

- the extent to which existing exclusions from scope of competition law apply for example to:
    - certain passenger services which could be classified as the performance of services of general economic interest[14] and;
    - agreements between passenger operators which (primarily to protect network benefits for passengers) are subject to legal direction either as a result of a licence or franchise obligation or to agreements covered by the terms of Council Regulation (EC) 169/2009 which removes from the scope of Article 101(1) agreements such as those promoting the standardisation of technical equipment or the co-ordination of timetables for through journeys.

Regulation will, for the time being at least, continue to have a role in the railways in:

- ensuring that passengers continue to see network benefits which might not otherwise be delivered in a vertically separated railway and where there are regionally based franchises;
- providing certainty and assurance for the dependent customers and funders of the national monopoly provider of the railway infrastructure;
- protecting taxpayers money by way of delivery of funded outputs;
- targeting the level of market power in a market and thereby encouraging effective competition to become established;
- continually driving down costs (where the prospects for effective competition are

[14] Though no undertaking in the rail sector has yet argued that it satisfies the criteria for it to be considered as performing such a task.

limited[15]) and provide a regulatory stimulus/incentives framework for better performance and efficiency; and

- regulating against exploitative behaviour in particular where the market alone will not deliver outcomes (including a price) which is compatible with economic growth.

Making competition powers easier to use

Our response is contained in comments relating to Chapters 3 and 5.

Strengthening the primacy of competition law over sectoral regulation

This should not make a significant difference to the way we do business currently but any measure adopted should not undermine the *Government's Principles for Economic Regulation* which establish the principle that regulators should be given discretion to act in a way that they consider most appropriate. Two principles are particularly relevant here:

- **Adaptability** – the framework of economic regulation needs capacity to respond to changing circumstances and continue to be relevant and effective over time; and

- **Focus** – economic regulators should have adequate discretion to choose the tools that best achieve [the protection of the interests of consumers and taxpayers].

We are happy to discuss a common set of factors with other regulators which set out the circumstances/factors where competition law would be used. In practice this might be difficult to achieve due to the differences between us in terms of the markets we regulate and our sector specific statutory frameworks.

Creating CM(A) as a central resource

Tremendous opportunities in the proposals here. There are clearly times where regulators would benefit from advice and resource from each other and from the CMA, particularly where cases are likely to lead into unprecedented case law. However this already happens, to some extent, through CWP and on a bilateral basis, for example:

- we have on two previous occasions seconded an OFT officer to assist on-site inspection and this worked very well from our perspective;

- we have had exchanges on matters of procedure (for example we discussed with

[15] "*In certain sectors network effects and/or economies of scale create circumstances, such as natural monopolies, which, under current technological patterns, limit the prospect for effective competition*" (paragraph 2 of the BIS Principles for Economic Regulation, April 2011

OFT our proposal to settle the EWS case by way of a settlement decision);

- our economists have had bi-lateral exchanges (for example, in developing an approach for assessing pricing complaints during periods of excess capacity; and to discuss our views on how competition law applies to franchised passenger services); and

- we hosted a joint regulatory workshop to discuss issues around services of general economic interest.

We would welcome more fluidity between us but this is inevitably going to be constrained by capacity and given that most investigations are re-active, the sharing of resource will be difficult to plan particularly during this period of public sector spending restraints and recruitment freezes.

Giving the CMA a bigger role in the regulated sectors

We have material concerns with these proposals and these are set out in the covering letter, in summary some of the proposals seem to establish in practice more than one regulator for the regulated sectors and this is not in accordance with Government's Principles for Economic Regulation particularly in terms of certainty and stability for business and the commitment not to erode the independence of regulators.

In preference we consider there is a case for much closer bi-lateral working relationships which could be of mutual benefit in sharing expertise and understanding.

We also have significant concerns around the proposal that the CMA be provided with an objective or duty to keep key sectors under review. Although we understand that there can be benefits from reviews being undertaken, from time to time, by a 'fresh pair of eyes', there are also countervailing risks which would need to be controlled such as:

- regulated sectors are already subject to a significant degree of scrutiny particularly at each pricing control period. In addition railways have recently been through the McNulty review. Markets need time to settle and to respond;

- the timing and frequency of such reviews would have to be thought through carefully in order to limit inevitable dampening effects on markets and to avoid unnecessary compliance costs; and

- the proposal (depending of course on the scale and scope and remedies attached to such reviews) could be considered disproportionate and surely should be triggered by at least a suspicion of harm.

Such arguments could equally be applied to such a duty being given to regulators.

In November 2006 the National Audit Office (NAO) published a report on the modernisation of the West Coast mainline. The report specified that in three instances

tenders for signalling contracts were let at around 20% above Network Rail's cost estimates.

Our closer scrutiny of the market (http://www.rail-reg.gov.uk/server/show/ConWebDoc.9566) demonstrated that a lack of stability and continuity in supply markets (due in this instance to the contracting strategy of Network Rail) had contributed to costs significantly in excess of estimates.

There could be similar effects where periodic and in depth scrutiny of markets dampens activity due to uncertainty particularly as to long term outcomes.

*Regulatory appeals and other functions of the OFT and CC*

This chapter sets out the Government's view that the sectoral reference/appeal jurisdictions of the CC should be transferred to the CMA. We also propose the development of model regulatory processes that set out the core requirements that future regulatory reference/appeals processes should have.

***Q.17** Do you agree that the CMA will be the most appropriate body for considering regulatory references/appeals currently heard by the CC?*

***Q.18** The Government also seeks your views on creating model regulatory processes that set out the core requirements that future regulatory reference/appeals processes should have.*

Comments: [Chapter 8 – Regulatory references and appeals]

We note that the preferred option is essentially to 'lift and shift' appeals currently heard at the CC to the newly merged CMA and there are various options in terms of how such appeals will be heard in the new structure.

ORR is interested from two perspectives:

- our ability to refer licence modifications to the CC under s13 of the Railways Act 1993 in the event that such modifications are not agreed by the licence holder; and
- our ability to refer our access charges review to the CC under paragraph 9 of Schedule 4A the Railways Act 1993.

As noted in the covering letter the consultation sets out various options for how such appeals will be heard in the new structure, although these are not fully developed. Our major concerns going forward are:

- that the panel appointed to hear such appeals is sufficiently separate so as not to appear biased by association with concurrent relationships (which is a concern with the preferred option); and of course
- that the panel has sufficient expertise to hear cases which given their statutory genesis will require understanding of a broad range of disciplines.

We are happy to discuss proposals as they develop but currently we are not persuaded that either of the CMA or the CAT would as proposed or currently structured necessarily address those concerns.

We are also happy to be part of an initiative for regulators to develop model regulatory processes for adoption over time but the challenge will be considerable given the significant differences in statutory frameworks.

*Scope, objectives and governance*

This chapter sets out that the CMA should have a primary focus on competition. The Government is committed to maintaining the independence of a single CMA and proposes that the CMA will: have clear, and potentially statutory, objectives to underpin prioritisation; be accountable to Parliament; and, have an appropriate governance structure for a single decision making body. We ask:

***Q.19** The Government seeks your views on appropriate objectives for the CMA and whether these should be embedded in statute.*

***Q.20*** *The Government see your views on whether the CMA should have a clear principal competition focus?*

***Q.21*** *The Government also seeks your views on the proposed governance structure and on the composition of the Executive and Supervisory Boards.*

Comments: Chapter 9 – Scope, objectives and governance.

We note in this Chapter (paragraph 9.21) the reference to the upcoming consultation on the reform of the consumer landscape We welcome the emerging view that sector regulators retain consumer enforcement powers in the new structure. We agree with the consultation that performing these functions in the regulated sectors ensures the application of specific expertise which would be lost by distributing the functions elsewhere.

We would add that our role as sector regulator provides us with the opportunity to take a national view which may not be possible should enforcement rest at local level alone. This is important in sectors, such as the railways, where network benefits are valued by passengers and where the harm may be systemic rather than contained to say a single train operating company.

*Decision making*

This chapter sets out a number of alternative models for decision-making that can deliver robust decisions through a fair and transparent process. The Government considers that a number of alternative models can deliver this, final choices will be guided by considerations relating to: the degree of separation between first and second phase decision making; degrees of difference or uniformity of approaches between tools; and, the role and nature of panels in the different tools available to the single CMA.

***Q.22*** *The Government seeks your on the models outlined in this Chapter, in particular:*

- *the arguments for and against the options;*

- *the costs and benefits of the regime and to business, supported by evidence wherever possible.*

***Q. 23** The Government also seeks views on the appropriate composition of the decision-making bodies set out in this Chapter, and in particular what the appropriate mix of full-time and part-time members is.*

***Q.24** The Government welcomes suggestions for alternative decision-making structures for each of the competition tools that will deliver robust decisions through a fair and transparent process.*

Comments: Chapter 10, decision-making

We set out our process for making decisions on anti-trust cases in our response to chapter 5. For completeness the management of our market studies programme is delegated to a programme board which has a cross-office representation and is chaired by a director. A decision on whether or not to refer a market (and to undertake the statutory obligation to consult on our intention) to the CC is a matter reserved to the ORR Board. Our practice has been to establish a sub-committee of the ORR Board to challenge our processes and emerging findings on markets where (such was the case in the referral of passenger rolling stock) we consider that a reference is becoming a real possibility and we are, for example, preparing to consult to that effect.

In order to respond fully to this chapter would require more clarity on how concurrent regulators are expected to fit into this structure of governance and how regulators will be expected to manage governance of future cases.

As noted in chapter 5 we would have to think through the implications of any proposals for a procedural and governance framework which were at variance with the established and agreed structures for the management and governance of our safety and economic functions.

*Merger fees and cost recovery*

Merger Fees

This chapter sets out options to recover the cost of the merger regime either by changing the level of the existing fee bands, introducing an additional fee band or moving to a mandatory notification system. We ask:

Q.25 **What are your views on options in this section or is there another fee structure which would be more appropriate and would ensure full cost recovery under a voluntary/ mandatory notification regime?**

## Recovering the cost of anti trust investigations

The Government is considering introducing legislation to allow the enforcement authorities to recover the costs of their investigations in antitrust cases. This would only apply where there has been an infringement decision and a fine, non-infringement decisions and investigations dropped for any other reason would not be charged. We ask:

Q.26 **Do you agree with the principle that the competition authority should be able to recover the costs of an investigation arising from a party found to have infringed competition law? If not, please give reasons.**

Q.27 **What are your views on recovery where there has been an infringement decision being based on the cost of investigation?**

Q.28 **What are your views on the recovery of costs in cases involving considerations of immunity, leniency, early settlement and commitments?**

It is foreseen that any costs to be recovered would be shown on the infringement decision detailing the fine. We ask:

Q.29 **Do you agree that this would be an appropriate way to collect the costs, separates the fine from costs in a way that makes appeals clear and that the costs should go to the consolidated fund rather than the enforcement authority?**

It is foreseen that the costs element could be appealed. This raises the question of what happens when the appeal is successful, partly successful or when the appeal is on the method of penalty calculation only rather than the substance of the decision. We ask:

Q.30 **Should a party who successfully appeals all or part of an infringement decision be liable for the costs element and should a party who appeals the method of penalty calculation, but does not appeal the substance of the enforcer's decision, be liable for a reduction in costs?**

Currently there is no legislation to allow the enforcer to charge costs so this would mean amending the Competition Act 1998. An alternative introducing cost recovery would be to amend the same Act to allow the level of fine to cover the cost of the investigation. We ask:

Q.31 **Should the Government introduce a power to allow the enforcer to recover their costs, or amend the Competition Act 1998 to enable the level of fine to cover the cost of the investigation rather than introduce costs?**

Recovery of CC costs in telecom price appeals

Q.32 **Do you agree that telecoms appeal should be treated in the same way as other regulatory appeals (e.g. Water Licence Modifications and Energy Price Control Appeals) in that the CC should have the ability to reclaim their own costs from an unsuccessful or partly successful appeal from the appellant at the end of the hearing? If not, your response should provide reasons supported by evidence where appropriate.**

Recovery of CAT costs

The Government propose to make a change in the CAT's Rules of Procedure to allow the CAT to recover its own costs following an appeal. The decision whether or not to impose costs will rest with the tribunal who will be able to set aside the costs where the interests of justice dictate e.g. when the appellant is a small business and the costs of pursuing their legal right of appeal prevent them from doing so. We ask:

Q.33 **What are your views on the proposal that the CAT recover their full costs except where the interests of justice dictate the costs should be set aside and what affect, if any, would there be on CAT incentives?**

Comments: [Chapter 11 – Merger Fees and Cost Recovery]

The following text is for information and to inform the discussion going forward. Our only comment about future cost recovery is that it is clear that any new system should remain mindful of small parties who may be disinclined to enter into proceedings where costs can be considerable. We note the proposed safeguards including the proposal to modify the Rules of Procedure (paragraphs 11.49-11.50) to provide greater flexibility to the CAT.

ORR's economic functions are funded by licence fee* and our safety functions are funded by safety levy on the industry. We have no separate funding for our competition functions and it is possible, therefore, that industry parties might prefer for costs to be recycled rather than sent to the consolidated fund.

*In addition to a licence fee, licence holders must also pay a contribution to any costs incurred in connection with licence modification references made to the CC by ORR (in relation to that licence) in the previous year. Where occurring, such costs are determined by ORR following discussion with the CC.

For safety enforcement, the court can order the defendant to pay the costs of prosecution (including the costs of investigation with a view to prosecution) where the prosecution leads to the defendant's conviction. The court's power to do so is the same as that in other criminal cases, namely the Prosecution of Offences Act 1985. The cost of serving an enforcement notice is not recoverable but if we successfully resist an appeal against a notice the employment tribunal has the power to order the duty holder to pay our costs (in most circumstances to a maximum of £10,000). The tribunal's powers are found in Schedule 4 of the Employment Tribunals (Constitution and Rules of Procedure) Regulations 2004.

## 12. Overseas information gateways

This chapter seeks views on how well the information gateway arrangements are working and whether there is a case for change. In particular, whether there is a case for amending the thresholds for disclosure of merger and markets information to promote reciprocity between overseas regulators and the UK and, if so, how this might be done. We ask:

Q.34 **How well is the current overseas information disclosure gateway working? Is there a case for reviewing this provision?**

Comments: [Chapter 12 – Overseas Gateways]

No comments here.

## 13. Questions on the impact assessment

Mergers

In this section we outline, and quantify where possible, the costs and benefits of the proposed options regarding strengthening the current voluntary notification regime, introducing mandatory notification, exempting small businesses from merger control, streamlining the merger process and adjusting merger fees.

Q.35 **Do you have any evidence about the costs to businesses of notifying mergers to the OFT, in terms of management time and legal fees?**

Anti-trust

In this section we outline the costs and benefits of the options for achieving a greater throughput of antitrust cases including enhancing the OFT's existing procedures, developing a new administrative approach and developing a prosecutorial approach. In addition we review the costs and benefits of retaining the 'dishonesty' element in the criminal cartel offence but exclude the possibility for defendants to introduce economic evidence produced after the events that constitute the alleged dishonest 'agreement'.

Q.36 **Under a prosecutorial system, are there likely to be changes to the overall costs of the system?**

The Impact Assessment presents the likely costs and benefits and the associated risks of the policy options. In order to do this it is necessary to understand the costs and benefits of the current system and to make assumptions. Further, the Impact Assessment seeks to show the extent to which the policy options meet the objectives.

Q.37 **Do you have better information about the costs and benefits of the current competition regime?**

Q.38 **Do you have evidence that indicates better assumptions could be made to estimate the costs and benefits of the proposed options?**

Q.39 **Are there likely to be any unintended consequences of the policy proposals outlined?**

Comments

No specific comments here over and above those already made in response to previous questions.