ALLEN & OVERY

Major reforms proposed for UK competition and consumer regimes, including digital

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In a move aimed at driving growth and delivering competitive markets that work for consumers, the UK government has published two consultations on proposals for reform of the UK competition and consumer rules. One – **Reforming Competition and Consumer Policy** – proposes general changes designed to ensure that the UK competition and consumer regimes are "best-in-class". The other focuses on the digital sector, and maps out the government's plans for a "**new pro-competition regime for digital markets**".

The consultations come on the back of a string of calls for reform, expert reports and advice received by the government in the past few years. These include **2019 proposals by the then Chair of the Competition and Markets Authority (CMA) Lord Tyrie**, **the Furman Report**, **John Penrose MP's review**, the **CMA's market study into online platforms and digital advertising**, and the **recommendations of the Digital Markets Taskforce (Taskforce)**.

The government has – broadly – taken heed of the proposals in these reports and has built many of them into its consultations. A number of the reforms were therefore expected. But in other cases the government plans to take a different approach, or has put forward new (and in some cases radical) changes. We take you through the headline points.

Wide-ranging reforms to the competition regime

The government points to evidence that competition in the UK may have weakened over the past 20 years, with markets becoming more concentrated. In its view, the changes proposed will create a competition regime fit for the 21st century and the digital age.

Merger control: significant threshold changes

The government is not minded to move away from the current voluntary and non-suspensory merger review process. But it believes the regime can be improved. Significantly, it proposes amending the jurisdictional thresholds by:

- Increasing the turnover threshold from **GBP70 million to GBP100m**, and creating a **safe harbour** which excludes from the CMA's jurisdiction mergers where each party's worldwide turnover is less than GBP10m. The changes are designed to provide greater comfort to small businesses and parties to mergers that are less likely to raise competition concerns.
- Introducing a **new threshold** enabling the CMA to review a transaction where any party has (i) a share of supply of at least 25% of any goods or services in the UK (or a substantial part of it); **and** (ii) a UK turnover of more than GBP100m. Here, the government's aim is to enable the CMA to review more easily vertical and conglomerate mergers involving large players, as well as "killer acquisitions" (ie purchases of start-ups or potential new entrants by larger players). This proposal is more controversial. If adopted it would bring a significant number of transactions into the CMA's remit (many of which may have no nexus to the UK). This is especially the case given the CMA's recent expansive approach to applying the share of supply test (**see our alert on Sabre/Farelogix**). This reform in particular is likely to face fierce resistance by the business community during the consultation process.

A more efficient merger control process is also a key aim of the proposals. The government puts forward a number of changes, including allowing remedies to be agreed earlier in a phase 2 investigation, reducing delays during a phase 2 review, and a new fast track route that would enable parties to request an automatic reference to phase 2 without the need for the CMA to undertake a competition assessment at phase 1.

Markets: more flexibility, more powers

The market inquiry regime enables the CMA to remedy harmful practices and structural barriers to competition across entire markets. It is a strong tool, and one that is largely unique to the UK. The government is concerned, however, that the current system – and in particular the in-depth market investigation process – is cumbersome and underused. It aims to inject flexibility into the regime and to give the CMA stronger powers by:

- Enabling the CMA to **impose remedies at the end of a first phase market study**. This would be a big change – currently the CMA can only accept undertakings offered by businesses at this stage. But it looks likely that this power would be limited to non-structural remedies, with the ability to require divestments reserved for use in in-depth market investigations only.
- Alternatively (and even more ambitiously), replacing the current two-stage system with a **new single market inquiry tool**, subject to a shorter overall timeline – two years (extendable by six months) – but within which the CMA would be expected to conclude investigations more quickly where appropriate.
- Allowing the CMA to impose **interim measures and accept binding commitments** from businesses at any point during a market inquiry.
- Giving the CMA **greater powers in relation to remedies** – both to monitor and review remedies imposed, and to more easily expand, supplement or revoke them.

Anti-competitive conduct: expanding territorial scope and incentivising leniency applicants

There are two significant proposals for reform of the rules on anti-competitive conduct:

- First, the government is proposing to **expand the territorial scope** of its rules on anti-competitive conduct by introducing an "effects" test. It wants the CMA to be "able to protect the UK's interests in globalised markets" and to align the UK laws with those of other jurisdictions such as the U.S. and EU. In practice, this would mean that the UK prohibitions on anti-competitive agreements and abuse of dominance would apply to agreements or conduct which, even if not implemented or occurring in the UK, have, or are likely to have, direct, substantial, and foreseeable effects within the UK.
- Second, changes to incentivise leniency applicants are suggested. The government is seeking views on the merits of **providing holders of full immunity in the public enforcement process with additional immunity from liability for damages** caused by a cartel. This would be a significant change, and one that appears to run counter to the EU Damages Directive (implemented into UK law). Under the Directive, while immunity applicants benefit from some protections from exposure, the basic principle is that they can face private damages actions. The proposed reform lays down a marker that the UK government is not simply prepared to stay in step with EU rules in the post-Brexit world.

On top of these reforms, the government suggests various changes to strengthen the CMA's powers to impose interim measures and to gather evidence. And it plans to streamline the settlement process as well as to introduce a new settlement tool for abuse of dominance cases, which it hopes would result in the more efficient completion of what are often complex and time-consuming investigations.

Finally, the government adds fuel to the fire of a long-running debate over judicial scrutiny of CMA decisions. It welcomes views on whether the current "on the merits" standard of review – which enables the Competition Appeal Tribunal to carry out an in-depth review of the law and facts – remains appropriate. Or whether such decisions should be subject to the lower level of scrutiny on judicial review grounds. Interestingly, while pointing out that businesses and their advisers appear to support the current system, the government does not set out its own preferred approach.

Tough sanctions for non-compliance across the board

For many years, the CMA has called for tougher powers to sanction companies for failing to comply with investigations. At the moment, penalties are capped at GBP30,000 (or a GBP15,000 daily rate). The government proposes a significant increase – fixed penalties of up to 1% of annual turnover and additional daily penalties of up to 5% of daily turnover while non-compliance continues – bringing the UK rules in line with the EU and other international equivalents.

Similarly, where companies fail to comply with remedies the CMA's current powers are limited to asking the court for an enforcement order. The government wants to enable the CMA to impose fixed penalties of up to 5% of annual turnover (and additional daily penalties of up to 5% of daily turnover).

If adopted, these amendments would significantly bolster the CMA's powers to enforce against procedural breaches. And we expect that the CMA would not be shy in making full use of them.

A more active role for government

More generally, the government is considering whether it should give more detailed and more frequent "strategic steers" to the CMA. These set out the government's expectations and priorities and are used by the CMA to set its own strategic priorities. The government wants to make sure that, with an expanded post-Brexit role, the CMA is guided to use its powers and tools to best effect. But it will need to be careful to balance this aim with ensuring the CMA retains its position as an independent authority. Importantly, therefore, the government notes that the steers will not bind the CMA. However, any departures from them will need explanation.

Enhanced consumer law enforcement

Both the Penrose review and Lord Tyrie's proposals recommended that the CMA's consumer law enforcement powers should be beefed up in line with its competition powers. The government has taken this advice on board.

Under the proposals, non-compliance with consumer law faces fines of up to 10% of global turnover. Plus there will be civil fines for businesses who refuse to give, or give misleading, information and financial penalties for breach of commitments. Significantly in terms of speed, the CMA will be able to enforce the law directly rather than through the lengthy court system.

The government is also considering ways to support consumers and traders to resolve more disputes independently, for example through arbitration and mediation. And is seeking views on making it easier for consumers to band together to collectively seek redress from traders.

A new bespoke digital markets regime

Alongside the broader competition reform proposals, the government has set out its much-awaited consultation on a new pro-competition regime for digital markets. The Digital Markets Unit (**DMU**), which was launched within the CMA in April 2021 and is currently working in shadow form, will enforce the regime. It will be responsible for designating firms as having "Strategic Market Status" (**SMS**), overseeing a mandatory code of conduct to which SMS firms will be subject, and implementing "pro-competitive interventions" (**PCIs**).

In the consultation, the government maps out its approach to each aspect of the proposed regime, seeking input on the details.

DMU: a duty to promote competition

The government's view is that the DMU's statutory duty should be to promote competition in digital markets for the benefit of consumers. Interestingly, the government rejects the Taskforce's proposal to include the "interests of citizens" in the DMU's duty, which could bring wider policy issues (such as data privacy) into consideration, instead favouring a "lean and simple" approach.

SMS: a cumulative test

The government proposes that in order to be designated with SMS a firm must satisfy two cumulative conditions:

- **It must have substantial and entrenched market power in at least one digital activity**. As the government notes, "substantial market power arises when users of a firm's product or services lack good alternatives…and there is a limited threat of entry or expansion by other suppliers". Entrenched market power occurs "once a firm's market power is expected to persist over time and is unlikely to be competed away in the short or medium-term". The government believes it is important that both elements are present for SMS designation. The regime will be limited to activities where digital technologies are a "core component" – there will be no need for the DMU to formally define markets.
- **This market power must provide the firm with a strategic position**, ie where the effects of the market power are likely to be particularly widespread or significant. The definition of strategic position and relevant assessment criteria are to be set out in the legislation.

The government proposes that the DMU uses a range of qualitative and quantitative evidence when carrying out SMS assessments. It moots a possible nine month deadline for the DMU to complete the assessment process (shorter than the 12 months proposed by the Taskforce), which will include a public consultation. SMS status would be in place for five years before being reviewed, although firms could request an earlier review.

Code of conduct: a flexible approach?

SMS firms will be subject to an enforceable code of conduct in relation to their designated activities. The code will set out how they are expected to behave. The government proposes that the code will consist of three high-level objectives (fair trading, open choices and trust and transparency). Legally binding principles would be derived from these objectives. Examples could include:

- Not to apply unduly discriminatory terms to certain users.
- Not to unduly influence competitive processes in a way that self-preferences.
- Not to bundle or tie in a way that has an adverse effect on users.
- Provide clear, relevant, accurate and accessible information to users.

One area up for debate is whether these principles are set out in legislation, or are to be determined by the DMU on a firm-specific basis, or a combination of these approaches. The government is minded to adopt the third option – a set of statutory principles with the DMU having power to develop additional firm-specific requirements in relation to those principles.

It is proposed that the DMU will be able to issue (non-binding) guidance to specific firms on how the code applies to them. And it will be able to enforce code breaches through orders, both interim and final.

Pro-competitive interventions: wide remedial powers

The government's intention is that the code will set out the "rules of the game" in advance, while the DMU will be able to impose PCIs to address the root causes of substantial and entrenched market power.

There are clear parallels here with the CMA's existing market investigations regime. The DMU would be able to implement a similarly wide range of remedies although, crucially, the government has not yet decided on whether certain interventions such as ownership separation should be excluded from the DMU's toolkit. This is likely to be a key focus for many respondents to the consultation.

And in order to be able to implement a PCI, the government proposes that the DMU must prove an adverse effect on competition, again in line with the legal test in a market investigation.

The DMU will be able to monitor, review and amend PCI remedies, and to accept voluntary enforceable undertakings from SMS firms during the course of an investigation. There will be a statutory deadline for completing a PCI investigation – the government seeks views on what would be appropriate, suggesting nine months with an optional three-month extension.

Unlike the code of conduct, which will broadly only apply to the designated activities of an SMS firm, the government intends that PCIs can be implemented anywhere within an SMS firm, provided the intervention is related to a concern in a designated activity.

Strict powers of enforcement

The DMU's enforcement powers will be tough: SMS firms that breach the code or fail to comply with code or PCI orders face fines of up to 10% of global turnover. The government is also considering holding senior managers liable for compliance with the regime, including through director disqualification. The DMU will have powers to gather information similar to those of the CMA and Ofcom, including the ability to conduct dawn raids.

Standalone merger control regime

The proposed new merger control rules applying to SMS firms are ground-breaking. The government plans to introduce a bespoke regime, applying across the whole firm, administered by the CMA. It would involve:

- A requirement for SMS firms to inform the CMA of **all** mergers, potentially in advance of completion, by providing basic information about the deal.
- In addition to the general jurisdictional thresholds, for mergers involving SMS firms, a **new threshold** would combine a transaction value threshold (possibly in the region of GBP100m or GBP200m) and a UK nexus test. The government wants to ensure that competitively significant mergers are caught. It is notable that the government looks set to follow in the footsteps of jurisdictions such as Austria and Germany that have already introduced transaction value thresholds. Other authorities, however, such as the European Commission, have declined to take this path.
- A subset of mergers by SMS firms could be subject to a **mandatory suspensory merger review**. This is a radical proposal. The government intends that this will catch deals which meet a transaction value threshold that is higher than the jurisdictional threshold mentioned above, although the consultation is silent as to the precise level.

And, in another significant proposal, the government believes it would be beneficial to change the substantive test for phase 2 merger investigations. It proposes applying a lower standard – a “realistic prospect” of a substantial lessening of competition – rather than the ‘more likely than not’ balance of probabilities standard. If adopted, this would be a major change, and one that would enable the CMA to take a much more interventionist stance when deciding whether to block a transaction.

Next steps

Taken together, the two consultations set out the most significant potential reforms to the UK competition and consumer regimes since the CMA was created in 2014. The government is inviting responses by 1 October 2021. We will update you with major developments as they occur.

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