Structural remedies:
A unique antitrust tool

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Injonction structurelle : Un instrument hors norme

THE USE OF DIVESTITURE REMEDIES IN UK MARKET INVESTIGATIONS: WHAT CAN BE LEARNT FROM THE BAA SAGA?

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1. Since the introduction of the Enterprise Act 2002 (the “EA02”) in 2003, the UK’s Competition Commission (the “CC”) has had the power to impose remedies where, following a reference from the Office of Fair Trading (the “OFT”), it concludes that features (or the combination of features) of a market give rise to adverse effects on competition. The so-called “market investigation” regime is not aimed at controlling illegal agreements or abuse of dominance under Articles 101 and 102 TFEU (and the UK equivalents) but rather enables the CC, on a reference from the OFT, to examine whether competition is weak or ineffectual in particular markets.

2. While the CC has imposed behavioural remedies in a number of market investigations, it has imposed divestiture remedies in only a single case to date. The case related to the supply of airport services by BAA, the largest airport operator in the UK. BAA had been privatised by the UK government in 1987 with a view to ensuring sufficient airport capacity and increasing airline competition. During the 2000s, the regulator, the Civil Aviation Authority, had permitted significant increases in airport charges (contrary to the CC's recommendations) ostensibly to allow for increased investment in capacity and security at the airports. The CC recognised that divestiture by BAA of three of its then seven airports constituted a major intervention in the market and would have significant ramifications for BAA’s business, while the scale and timing of customer benefits were not certain. The CC nevertheless considered that the detrimental effects identified were long-standing and went to the heart of the structure of the market (with BAA in effect holding a monopoly position in London). The CC also considered that the market characteristics underpinning the adverse effects on competition would unlikely change absent divestiture. The decision was controversial for a number of reasons, including the unprecedented nature of the remedies and the fact that the action was taken after BAA had been acquired by a consortium led by the Spanish infrastructure group Ferrovial.

3. This article considers in the context of UK market investigations the use of divestiture remedies prior to the EA02 (I.), the general approach to remedies under the EA02 (II.), the BAA case (III.), and the choice of behavioural remedies over divestiture in other cases (IV.). Section V provides concluding remarks.

I. Position prior to the EA02

4. Before the EA02, the CC and its predecessor body, the Monopolies and Mergers Commission (the “MMC”), had been entitled to recommend action to the UK government pursuant to a market investigation but could not impose remedies. The MMC had recommended divestitures in a very small number of cases, although its recommendations were not always followed. An example of where the MMC’s recommendations were followed is the supply of beer market investigation in 1989. In that case, the MMC recommended that brewers should not be allowed to own more than 2,000 on-licensed premises. At the time, six large brewers owned almost 75% of public houses in the UK and were protected from competition in supplying their managed and tenanted estates because other brewers did not have access to them except for a “guest beer” provision. Brewers also often had influence over many of the remaining “free houses” through exclusivity arrangements, thereby further reducing competition. The MMC estimated that its recommendation would lead to divestiture of 22,000 on-licensed premises by the larger brewers. This remedy arguably contributed to the closure of many pubs, which now need to share their profits with both a brewer and a landlord.

II. General approach to remedies under EA02

5. Pursuant to section 134 of the EA02, where the CC finds an adverse effect on competition following a market investigation, it must decide whether (and what) action should be taken for purposes of remedying the adverse effect or any detrimental effect on customers resulting from the adverse effect. In reaching its conclusion, the CC must have regard to the need to achieve as comprehensive a solution as is reasonable and practicable.

60 The OFT can accept remedies in lieu of reference to the CC.

61 This article does not consider remedies in the UK for breaches of Article 101 and 102 TFEU (and the UK equivalents) or in the merger context.

62 Beer Report, March 1989. Other market investigations in which the MMC recommended divestiture remedies (or remedies analogous to divestiture) include: (1) Animal Waste Report, September 1993 (divestiture of rendering facility to stimulate new entry); (2) Certain Gas Domestic Appliances Report, 29 July 1980 (forced withdrawal of British Gas Corporation from the retailing of gas appliances in the UK); and (3) Cigarettes and Tobacco Report, 4 July 1961 (divestiture by Imperial Tobacco, accounting for over 60% of cigarette and tobacco sales in the UK, of its 42.5% shareholding in Gallaher, its trading competitor). This does not include market investigations that were in effect reviews of completed mergers.
6. When considering remedies, the CC considers the effectiveness of different remedies and their associated costs, always subject to the principle of proportionality.63 The CC considers that one-off structural remedies have advantages compared with behavioural remedies since they address the competition concerns directly and require little monitoring.64 The CC will listen to proposals from the parties, although it will impose the remedy it deems effective.

7. The CC’s general approach to remedies can be compared with that of the European Commission (the “EC”) when imposing remedies for breaches of Article 101 and 102 TFEU. (The EC does not have power to order remedies when conducting sector inquiries, although it can open antitrust investigations on the back of sector inquiries that could in principle lead to remedies.) While the EC has the power to impose behavioural and structural remedies in antitrust cases, structural remedies should only be imposed either where there is no equally effective behavioural remedy or where any equally effective behavioural remedy would be more burdensome for the undertaking concerned than the structural remedy.65 To date, only three EC antitrust investigations (relating to gas and electricity markets) have resulted in divestiture remedies. The emphasis on behavioural remedies as the starting point for the EC is arguable different from the CC’s approach, as well as being the reverse of the EC’s (and CC’s) approach in merger cases where divestiture remedies are the starting point and strongly preferred.

III. BAA case

1. Overview of BAA case

8. The BAA case involved somewhat convoluted proceedings. Following a reference from the OFT on 29 March 2007, the CC concluded in its report of 19 March 2009 (the “2009 Report”)66 that there were adverse effects on competition in relation to the supply of airport services by BAA arising from BAA’s common ownership of airports in south-east England (Gatwick, Heathrow, Southampton, and Stansted) and lowland Scotland (Aberdeen, Edinburgh, and Glasgow), together with Heathrow’s position as the only major UK hub, aspects of the planning system, government policy, and the existing regulatory system. BAA accounted for more than 60% of all passengers using UK airports, rising to 90% in south-east England and 84% in Scotland. After identifying a significant degree of competition between non-BAA airports in the UK, the CC considered that there was potential for significant competition between BAA-owned airports (including as regards development of new runway capacity) and that common ownership by BAA was preventing such competition. The CC required a package of remedies, including divestiture of both Stansted and Gatwick airports to different purchasers, and the divestiture of either Edinburgh or Glasgow airport.

9. On 21 December 2009, the Competition Appeals Tribunal (the “CAT”) overturned the CC’s decision in light of apparent bias.67 BAA nevertheless failed in its arguments that the CC had not taken account of material considerations when assessing the proportionality of the divestitures. On 13 October 2010, the Court of Appeal (the “CA”) overturned the CAT’s judgment, thereby restoring the CC’s original decision.68

10. After remittance of the case, the CC subsequently determined on 19 July 2011 (the “2011 Report”)69 that there had not been any material change of circumstances since preparation of its 2009 Report and that it otherwise had no special reason for deciding the matter differently.70 Accordingly, BAA was required to proceed with the divestitures.71 Subsequent appeals by BAA against the 2011 Report were rejected by the CAT on 1 February 201272 and by the CA on 26 July 2012.73

11. As well as being the first case in which the CC has imposed divestiture remedies, the case raises a number of interesting aspects, including the circumstances in which the CC will impose structural rather than behavioural remedies, the CC’s approach to proportionality, and the time period permitted for divestitures.74

2. Choice of divestiture over behavioural remedies

12. In its 2009 Report, the CC found common ownership of the airports to be responsible for preventing competition between the airports in question and that a divestiture remedy would act directly and structurally on the adverse effect on competition. The CC likened the situation to a completed

64 C3, § 4.15. In terms of the effectiveness of any remedy, the CC considers the prospects of implementation and compliance, as well as the extent of monitoring required and how quickly the remedy can take effect (C3, § 4.10).
66 Airport Services by BAA Report, 19 March 2009.
merger and commented that such high market shares would not be tolerated, particularly where there were high barriers to entry. The CC noted that divestiture or prohibition has been required in over 80% of merger cases under the EA02 in which the CC has found a substantial lessening of competition and in virtually all cases where divestiture (or prohibition) has been feasible.

13. BAA argued that a requirement to lower prices in off-peak periods could be used instead of divestiture of either Gatwick or Stansted to address the potential price for encouraging greater use of capacity in off-peak periods. The CC nevertheless did not view spare runway capacity, the size of which depends on the efficiency of runway utilisation, as a factor that could facilitate competition between airports and thereby ensure the best possible outcomes for customers. BAA also considered that investment in new capacity could be achieved through regulation that increased investment incentives, but the CC thought that the regulatory system would be a poor “ mimic of competitive rivalry.”

3. Proportionality of divestiture remedies

14. A good deal of the legal argument in the BAA case both before the CC and the courts focused on issues of proportionality. When considering proportionality, the CC takes into account the costs of implementing and complying with a remedy. However, the CC also considers the wider picture and the fact that an adverse effect on competition is likely to result in a cost or disadvantage to the UK economy in general and to customers in particular.

15. Shortly before the 2009 Report, the CAT had set out the legal principles to be applied by the CC when considering proportionality. Referring to a European Court of Justice judgment, the CAT explained that the measure in question: (a) must be effective to achieve the legitimate aim in question; (b) must be no more onerous than is required to achieve that aim; (c) must be the least onerous, if there is a choice of equally effective measures; and (d) in any event must not produce adverse effects which are disproportionate to the aim pursued.

16. In the 2009 Report, the CC estimated the cost of divesting the three airports at £63 million, which was small relative to the turnover of the airports and their market value. The CC was in any event not minded to take into account the one-off cost of divestiture since BAA’s current owner had purchased BAA after the OFT had announced that it would conduct a market study. In terms of customer benefits arising from the features causing the adverse effect on competition, the CC believed that annual savings of £23 million from economies of scale from common ownership would only be passed onto consumers if there was effective competition or perhaps through regulation. The CC found on the other hand that customer benefits from the divestitures would be substantial and far outweigh the costs to BAA.

17. The CC did nevertheless acknowledge that calculating divestiture benefits is complex and subject to uncertainty. The difficulty of assessment in this case was compounded by the current lack of competition between the airports and the lack of comparators. The CC calculated that cost savings to customers would exceed the cost of divestiture, while divestiture would also give rise to new services and, in the longer term, capacity expansion and service levels being more closely aligned with customer interests.

4. Time permitted to complete divestitures

18. In terms of timing of the divestitures, the CC in the 2009 Report balanced the interests of resolving the adverse effects on competition promptly and avoiding deterioration of the businesses being divested against providing sufficient time to attract suitable purchasers which would not sell the airports in the short term. The CC accepted that a period longer than six months (i.e., the period normally applied in merger cases) should be permitted, not least given the difficulty of financing airport acquisitions during the financial crisis and the fact that airports are unlikely to deteriorate as quickly as other businesses over the divestiture period. The CC also accepted that it would be better to permit a sequential marketing of the airports in part because of the inability of bidders to mount effective bids concurrently and the limited capital availability in the financial crisis. While the precise divestiture timings are redacted from the 2009 Report, the CC stipulated that the divestitures overall must be completed within two years. Notwithstanding the fall in profitability at Stansted – it did remain profitable, the CC equally considered at the time of the 2011 Report that the divestiture timescale should not be lengthened.

19. Gatwick airport was sold to Global Infrastructure Partners (“GIP”) in December 2009, around the time of the 2009 Report. BAA subsequently sold Edinburgh airport (also to GIP) in April 2012 during BAA’s appeals against the 2011 Report. BAA sold Stansted to Manchester Airports Group in January 2013, around six months after it ended its legal challenges and over three years after the 2009 Report.

20. In its appeals before the courts, BAA argued that the CC should also have taken into account the loss to shareholders from a quick sale of Stansted in depressed market conditions. Both the CAT and the CA disagreed. The CAT held that,
where the CC concludes that divestiture is appropriate having taken into account the relevant proportionality principles and gives the company an appropriate opportunity to obtain a fair market value for its assets, the company’s interests will have been sufficiently taken into account and protected. There was no need for the CC to have had regard to a price that BAA might obtain in future or the revenues that BAA might obtain in future if, absent a divestiture requirement, it chose not to sell Stansted at all. The CAT found that the fair value of Stansted should be assessed by the value the market will pay for it after there has been a proper opportunity to market it.

IV. Choice of behavioural remedies over divestiture in other cases

21. In all market investigation cases in which the CC decides that remedies are required, it must consider whether structural remedies would be appropriate. In many cases, this will not require more than cursory consideration by the CC but the CC has examined the issue in more detail in a few cases.80

22. In its local bus services market investigation in 2011,81 the CC concluded that concentration levels were high and competition was not effective between bus operators in 239 cities or towns in the UK, with high entry barriers and operators lacking any incentive to participate in multi-operator ticketing schemes. The CC considered that divestitures would not be workable given the extremely large number of local markets raising adverse effects on competition, the widespread nature of the features identified as giving rise to the adverse effects, and the practical difficulties associated with evaluating and implementing divestitures in more than a small number of local markets. The CC made a number of recommendations, including legislative changes to increase multi-operator ticketing schemes, review of the Public Transport Ticketing Block Exemption, granting access to bus stations on fair, reasonable, and non-discriminatory terms, and imposing restrictions on bus operators making changes to service frequency.

23. In the groceries market investigation in 2008,82 the CC found that competition was restricted through larger supermarkets having high levels of concentration that had persisted over a number of years. In rejecting divestiture remedies, the CC noted that such remedies represent a very significant intervention in property rights, that transferring existing trading stores could have a disruptive effect on consumers in the short term, such intervention was not supported by the gravity and prevalence of the adverse effect on competition,83 and store divestitures in highly concentrated local markets would not effectively address concentration but comprise only a very limited and one-off intervention in a large and dynamic sector.84 The CC instead recommended a competition test in planning decisions (to avoid land banking by retailers), a requirement on grocery retailers to release restrictive land covenants and exclusivity arrangements in high concentration areas, creating a new Groceries Supply Code of Practice, and establishing an ombudsman to arbitrate on disputes under the Code.

24. In its market investigation into banking services to small and medium-sized enterprises (“SMEs”) in 2002,85 the CC examined a number of markets, including bank accounts, overdraft facilities, and business loans. The CC found significant market concentration, high entry barriers, a reluctance on the part of SMEs to switch banks, limited price sensitivity among SMEs, and lack of transparency. While the CC thought that behavioural remedies aimed at reducing entry barriers86 would not have sufficient impact on competition within the short term (not least given customers’ inertia to switching), the CC decided that structural remedies would not be appropriate. Obstacles to structural remedies included the need for wide-scale divestitures and the fact that they would affect personal customers who were outside of the terms of reference to the CC. Customers of branches could not be required to switch banks and so divestiture of branches would not overcome the problem facing new entrants, which need a sizeable customer base to be profitable.

25. It does appear that divestiture remedies would have been difficult to implement in these three cases and certainly difficult by comparison with the situation in the BAA case where a single company, which had recently led a consortium to acquire the airports in question, owned a small number of self-standing airports. This highlights further that the remedy in the BAA case is somewhat of an outlier.

V. Conclusion

26. The UK is unusual in having a regime that permits imposition of structural remedies following a market investigation as opposed to such intervention in the case of mergers or for illegal conduct. The BAA case involved a particularly significant and wide-ranging remedy package, with the businesses for divestiture selling for more than £3.5 billion. It is unlikely that a requirement to divest businesses on this scale would have gone unchallenged before the courts, particularly when this was the first remedy of its type under the EA02. The CC’s two decisions in this case nevertheless

80 For an example of a case prior to the EA02 where the MMC considered but rejected a divestiture remedy, see Classified Directory Advertising Services Report, March 1996. For an example of such a case before a sector regulator in the UK, see Strategic Review of Telecommunications by OFCOM, 22 September 2005.
81 20 December 2011.
82 30 April 2008.
83 The CC found that land banking and use of restrictive covenants and exclusivity arrangements by incumbent supermarkets acted as a barrier to entry to potential new larger stores. The CC also concluded that purchasing power by certain grocery retailers was uncompetitive.
84 The CC instead recommended a competition test in planning decisions, a requirement on grocery retailers to release restrictive land covenants and exclusivity arrangements in high concentration areas, creating a new Groceries Supply Code of Practice, and establishing an ombudsman to arbitrate on disputes under the Code.
85 March 2002.
86 The CC focus on enabling fast error-free switching between banks, limiting bundling of services, and to improve information and transparency.
withstood well the scrutiny of the courts. Proportionality was an important part of the appeals before the CAT and CA, but the courts upheld the CC’s decisions on that front. This will no doubt embolden the CC (and its successor body, the Competition and Markets Authority) when it determines that divestiture remedies are an appropriate way to resolve competition concerns in market investigations in future. Based on the small number of market investigation cases that have led to divestiture remedies in the past (including cases prior to the EA02) and the *sui generis* nature of the issues in the BAA case, it is not expected that divestiture remedies will become prevalent in such investigations. However, now that the CC has used divestiture, it is a more credible threat in future that could help to persuade parties to offer more effective alternative remedies.