
Reforming Competition Law in the UK: The Competition Act, 1998

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Abstract

The 1998 Competition Act introduced important changes to UK competition policy after years of concern that UK competition law was in need of reform. The new Act harmonises UK law with European Union legislation on restrictive practices and abuse of a dominant position. At the same time, UK competition policy retains certain features that continue to make it distinct from EU law and practice, especially in relation to the treatment of oligopoly and the regulation of mergers.

This paper details the changes to competition policy introduced by the 1998 Competition Act and reviews in particular the government's new powers of investigation and the penalties that can now be levied for anti-competitive behaviour. The paper also discusses the role and structure of the new Competition Commission. Where relevant comparisons are made with European Union policy.

1. Introduction²

COMPETITION BRINGS BENEFITS to consumers in terms of choice and lower prices but market economies are prone to anti-competitive behaviour because of market dominance and restrictive practices. To prevent competition from being undermined, many countries have adopted laws aimed at restricting such behaviour. In Europe Articles 81 and 82 of the EC Treaty (formerly articles 85 and 86³) provide powers to DG IV of the European Commission to tackle cartels and abuse of market dominance respec-

tively. In the UK the first legislation preceded the Treaty when, in 1948, the Monopoly and Restrictive Practices (Inquiry and Control) Act established a Monopolies Commission to investigate anti-competitive behaviour. In 1956 the regulation of restrictive practices was removed to a separate Restrictive Practices Court and in 1965 the Monopolies Commission's brief was widened to review mergers and takeovers. Two important pieces of legislation followed, in 1973 and 1980, aimed at strengthening competition law. In 1973 the Fair Trading Act established an Office of Fair Trading (OFT) within government, headed by a Director General of Fair Trading (DGFT). The OFT undertakes the scrutiny of competition within markets and has advised the Secretary of State of the Department of Trade and Industry (DTI) on possible referrals to the Monopolies and Mergers Commission. The 1980 Competition Act extended the work of the MMC to cover public bodies including the nationalised industries and extended the DGFT's powers to investigate anti-competitive practices.

During the 1980s there was growing pressure within government and outside to strengthen UK competition legislation and make it consistent with EU law. In a White Paper, in July 1989, the government proposed legislation that would realign UK policy with Article 81 on restrictive practices (DTI, 1989). However, the legislation was not forthcoming, officially because of congestion in the government's legislative timetable (DTI, 1992, p.1). In November 1992 a government Green Paper (consultative document) outlined alternative changes to the control of monopolies to make UK law more consistent with

Article 86 (now Article 82) on the abuse of dominance (ibid.). But in April 1993, with no consensus on the best way forward, the Government announced that the existing policy would be maintained. This was followed by further proposals for reform in 1996 (DTI, 1996).

In spite of the importance attached to competition by Conservative Governments, crowded parliamentary timetables plus some hesitancy to meddle with the existing legislative régime meant that competition law in the UK remained essentially unchanged until the arrival of a Labour Government in May 1997. The new Act received the Royal Assent on 9 November 1998; the Competition Commission was established on 1 April 1999; and a new prohibition-based policy aimed at outlawing anti-competitive behaviour takes effect from 1 March 2000.⁴

This paper details the changes in competition policy introduced by the Act in the light of existing European Union law on competition. The contents of the Act are likely to be far reaching, and yet its terms and scope are not yet well understood. The aim of the paper is to provide a readily accessible but comprehensive review of the provisions of the new Act and its likely impact.

2. The Main Features of the Competition Act

The new Competition Act repeals the Restrictive Trade Practices Act 1976, the Restrictive Practices Court Act 1976, the Resale Prices Act 1976 (which first prohibited individual resale price maintenance) and the Restrictive Trade Practices Act 1977. It also replaces Sections 2 to 10 of the Competition Act 1980 relating to the control of anti-competitive practices and introduces consideration of European competition law principles when interpreting the prohibitions under the Act. The Act is divided into two main Chapters: Chapter I of the Act deals with anti-competitive agreements and concerted practices and Chapter II with the abuse of a dominant position. The result is two prohibitions that replace the previous, more discretionary approach to

dealing with restrictive practices and market dominance in the UK.

The new Act also introduces a change in the administration of competition policy. It replaced the long-standing Monopolies and Mergers Commission (MMC) with a new Competition Commission (CC), with effect from 1 April 1999. But this change is not quite as significant as it might seem at first because the CC has inherited the personnel and functions of the MMC. The previous chairman of the MMC, Dr Derek Morris, has become the first chairman of the CC, and the MMC secretary and other staff have transferred to the new Commission. Similarly 'Members', who sat on MMC enquiries into monopolies and mergers and reviewed disputed licence amendments in the regulated utility sectors, have become Members of the CC. Their role and their method of appointment have been unaffected.⁵ The new CC has, however, taken on an 'appeals' function that the MMC did not have and this is important. The new Commission is therefore divided into two parts, one dealing with the traditional reporting duties (called the 'reporting side' of the Commission) and the other with appeals (in the form of Appeal Tribunals).

Reporting function

The 'reporting side' of the CC has a large number of different functions called in the Act 'the general functions of the Commission'. These are largely derived from the Fair Trading Act 1973 and privatisation statutes and are concerned with monopolies, mergers and regulatory inquiries. As before, the inquiries will be conducted by panels of four or five Members of the Commission with the following time limits applying - normally three months for mergers or newspapers inquiries and six months for a utility case.⁶ Monopoly references will, as before, take longer and normally be of between 9 and 12 months. Given that the Competition Act introduces a prohibition of monopoly abuse, it might be expected that the 'general functions' concerned with monopolies

will decline. However, since in recent years much of the MMC's time has been taken up in investigating what are known as 'complex monopolies', involving firms possibly acting together to reduce competition in the absence of a formal agreement (e.g. in the beer and motor trades, domestic electrical goods, and petrol), in practice this area of work may continue much as before. Monopoly enquiries will be referred to the CC, as was the case for inquiries by the MMC, by the DGFT subject to a veto by the Secretary of State for Trade and Industry, who may make references on his own initiative. The Commission will also continue to have jurisdiction over mergers but, as in the past, only in so far as they are referred to it by the Secretary of State.⁷ The Commission still does not have the authority to initiate its own inquiries. The government has signalled, however, its intention to move towards a situation where most merger decisions are taken by the competition authorities not ministers and where the test is competition rather than other issues (DTI, 1999). The government has intimated that it would like to see more of the discretion within UK competition policy transferred from the politicians to the competition authorities.⁸ Further reform in this area is therefore likely.

The Appeal Tribunal

An important institutional change introduced by the Act is the establishment of Appeal Tribunals within the Commission with an equivalent status to the High Court. The Tribunals are to be headed by a legally qualified President with the same status as a High Court judge. Each Tribunal will also consist of a legally qualified chairperson (who may be the President) and two lay-members, drawn from an appeals panel of members of the Commission.⁹ More than one Tribunal may sit at any one time. Judge Christopher Bellamy QC, currently a judge at the Court of First Instance of the EC, has been appointed the Tribunal's first President. The list of appealable decisions is wide, including errors of fact and law and the

DGFT's use of his discretionary powers. For example, the Tribunals will consider appeals against decisions by the DGFT on an infringement under Chapters I and II, directions to end an agreement or conduct under Sections 32 and 33 of the Act, and the granting of individual exemptions and interim measures under the terms of the Act. It will also review penalties levied by the DGFT for infringements under the Act in so far as firms appeal against the amount.¹⁰ Penalty appeals may form much of the work of the Tribunal, although this will probably depend upon the decisions reached by the Tribunal on the first few cases heard. If the Tribunal adopts a hard line on penalties then it is to be expected that more firms will shun appeals. The Appeal Tribunal will also hear appeals from decisions made by the specialist utility-sector regulators using their 'concurrent powers' under the Act. This is discussed more fully below.

The role of the Tribunal is to hear appeals based on the evidence already prepared by the DGFT and the parties involved and used in arriving at the initial decision. The Tribunal will not undertake investigations. Where it considers further information is necessary, it can either refer the matter back to the DGFT or ask for the evidence to be supplied. Appeals will be brought by those affected by a decision of the DGFT, notably undertakings that have been party to an agreement, or dominance, and also any other party that has a sufficient interest in the matter; this could for example include suppliers or consumer groups (Sharpe, 1999). Appeal from a decision of the Appeals Tribunal is permitted under the Act only on a point of law arising from the decision or over the amount of the penalty. Appeal is with leave and to the appropriate court - in England and Wales and Northern Ireland the Court of Appeal and in Scotland the Court of Session.¹¹

Powers of investigation

The Act gives the DGFT considerable new powers to tackle anti-competitive behaviour, similar

to the powers that the DGFT has when investigating breaches on behalf of the European Commission. Previously the DGFT's powers of investigation were limited, especially where undertakings obstructed the enquiries. The Act gives the OFT the following new powers of investigation (OFT, 1999a):

- to demand specified documents and information and to require explanations from company officers and employees;
- to mount 'dawn raids' using powers modelled on the European Commission's procedures. The DGFT can authorise inspectors to enter premises, request and copy documents and seek answers. Organisations suspected of being a party to an illegal agreement need be given no warning. Domestic premises can be entered if business documents are kept there;
- the OFT can ask a judge for a search warrant where it thinks that documents have been withheld or might be concealed or destroyed. Under this power reasonable force may be used and documents may be seized;
- obstructing an investigation is now a criminal offence punishable by an unlimited fine (this, incidentally, appears to go beyond the powers under European Commission procedures);
- obstructing an officer armed with a warrant, concealing documents or providing false or misleading information to the DGFT, is now deemed a criminal offence punishable by a fine or imprisonment of up to two years.

Also, the DGFT has been given powers to stop anti-competitive agreements or monopoly abuse pending completion of his investigations. These powers will be used where the DGFT reasonably suspects that abuse has occurred and where he considers that an order is necessary to prevent serious or irreparable damage to either the public interest or the interest of specific third parties. In all cases appeals against the decisions of the DGFT will be made to the Appeal Tribunal. It is

expected that undertakings appealing against the DGFT's decision will do so on the substantive findings or to challenge the penalties levied; however some appeals on procedural grounds may occur.¹²

Under the previous competition law no conduct was unlawful until after it had been proscribed by an order of the Secretary of State for Trade and Industry or after the firm concerned had given a legally binding undertaking to the DGFT that it would refrain from anti-competitive conduct. Therefore no penalties could be levied for previous conduct, no matter how damaging to competition, and the injured parties had no right to obtain damages for past injury. Under the new law the powers of the DGFT are considerably enhanced (OFT, 1999b). Firstly, infringements of the prohibitions under the 1998 Act can be brought to an end immediately on the issuing of an order by the DGFT following an investigation. This is a major change compared with the previous régime where adverse findings rarely led to direct bans. Secondly, extensive penalties can be levied by the DGFT for past and current infringements. Thirdly, where appropriate the DGFT will be able to impose interim measures to bring an immediate end to anti-competitive behaviour while an investigation is underway. In the past firms could go out of business while the competition authorities conducted their enquiries (as has occurred, for example, in bus transport).

Previously penalties could only be levied where there was a breach of an order. Now the DGFT can impose penalties where he is satisfied that an infringement of the Act was committed either intentionally or negligently. This again brings UK competition policy into line with EU law. The penalty levied will be up to 10 per cent of UK turnover,¹³ a level consistent with EU practice, which involves a 10 per cent threshold but on world-wide turnover. The penalties may, therefore, prove to be heavy and this is intentional to deter anti-competitive behaviour. Such incentive was missing under the previous régime. The Act

does contain de minimis limits to exempt 'small agreements' or 'conduct of minor significance' from the scope of the Act and this is expected to be of benefit to many SMEs. In other cases, however, only when it can be demonstrated that the party or parties acted erroneously but on a reasonable assumption that the conduct or agreement fell under the exclusion headings will no grounds for a penalty exist.

In addition to the penalties that can be imposed by the DGFT, for the first time third parties appear to have a civil right of action for damages suffered where parties claim that they have been victims of anti-competitive behaviour. Although no specific provision to that end exists in the Act, Ministers admitted that it was a possibility during the parliamentary debates. Actions for damages will be heard in the courts and a decision by the DGFT or the Appeal Tribunal is likely to be admissible as evidence in such an action. It is expected that the DGFT will disclose relevant material to third parties, except where this involves a breach of confidence, in an effort to encourage successful actions and thereby further deter anti-competitive behaviour.

Section 60 of the Act makes clear that when the DGFT makes decisions under the Act this should be done in a manner consistent with Community Law. Hence the EC Treaty and decisions of the Court of Justice must be followed. The DGFT, the CC and the UK courts will therefore have to have regard to past and future decisions of the European Commission and the European Court, including any 'Statement' of the European Commission. Also, the Secretary of State has powers to set priorities for the DGFT and can exclude actions under the Act on public policy grounds. The current Secretary of State, Stephen Byers, has announced that he intends to use his powers to set priorities where the government is keen to see action to raise competition (statement by the Secretary of State 10 March 1999). In sum, the scope of the new Act and its impact will only become fully apparent over time and will be sub-

ject to the decisions of the competition authorities, the Appeals Tribunals and the European Commission.

3. Regulating Restrictive Practices

As already explained, the Competition Act divides anti-competitive behaviour into two Chapters: Chapter I deals with restrictive practices and Chapter II with the abuse of a dominant position. The Chapters are now discussed.

Under the 1956 Restrictive Trade Practices Act and subsequent amending legislation cartel agreements were not prohibited they were simply 'registrable'. Once an agreement was registered the DGFT was required to bring the agreement before the Restrictive Practices Court. The onus was then on the parties to the agreement to establish that it was in the public interest in the context of certain 'gateways' laid down in the 1956 Act. In practice, over the years the Court took a tough line and few agreements received a favourable judgement. In consequence, most agreements were abandoned or heavily modified before the Court hearing. Where cases did get to Court, hearings could be lengthy and expensive. This provided a further disincentive to proceed to a full hearing.

Nevertheless, while the 1956 Act appeared to curb restrictive practices, the legislation had important loopholes. In particular, policy was based on ensuring registration of potentially anti-competitive agreements rather than preventing or detecting them. Also, it left open opportunities to avoid registration, for example by designing agreements where only one party accepted a restriction on its conduct. To be registrable agreements had to be accepted by two or more parties. Most importantly, however, there was no provision for retrospective penalties. This meant, therefore, that when unregistered restrictive practices were discovered penalties could not be imposed nor were damages recoverable under UK law (penalties under EU law apply only to restrictive practices which affect trade between member

states). Cases such as the secret price fixing agreements in the ready-mixed concrete industry, revealed in 1991, emphasised the weakness of the régime.

The 1998 Competition Act replaces the need for registration with a general prohibition. Chapter I of the Act sets out the prohibition against agreements between undertakings or concerted practices which 'may affect trade within the United Kingdom' and 'have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom' (Section 2(1)). Concerted practices involve collusion falling short of a formal agreement. The Chapter provides a list of agreements, decisions and concerted practices. This is intended to be illustrative and non-exhaustive and the wording is identical to that of Article 81(1) of the EC Treaty:

- (a) directly or indirectly fix purchasing or selling prices or any other trading conditions,;
- (b) limit or control production, markets, technical development or investment;
- (c) share markets or sources of supply;
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

As a result of the Act, all agreements that fall within the prohibition are void where they have a significant or appreciable effect on competition. Price fixing, output restrictions, investment restrictions, collusive tendering etc all appear to fall within the prohibition, although there are some exceptions. To explain how the OFT will interpret the Act, the DGFT has issued draft guidelines. These state that an agreement between parties with a combined market share of less than 25 per cent (known as 'small agreements') will

not normally be sufficient to amount to a significant effect unless they involve the fixing of prices.¹⁵ In other words, all price fixing agreements are caught no matter their size.

As under Article 81, parties to an agreement will be able to apply for clearance of an agreement. This will be made to the OFT and may take the form of 'informal guidance' (akin to the European Commission's 'comfort letter' and similarly not legally binding) or a 'formal decision' (following soundings from third parties and involving a detailed consideration of the agreement and the market). The same procedure applies for clearance under Chapter II of the Act relating to market dominance, discussed below.

One particular area of interest concerns vertical agreements, where economists are divided on the competitive effects (Neven, Papandropoulos and Seabright, 1998). The net welfare effects of vertical agreements depend particularly upon the relative importance of *intra* as against *inter*-brand competition. Intra-brand competition occurs between downstream producers or distributors in the resale or further processing of a given branded product. An exclusive distribution arrangement or the imposition of a minimum resale price will prevent, distort or reduce intra-brand rivalry. However, if an arrangement enables brand X to compete more effectively with other brands then inter-brand competition is enhanced. As a general principle, both UK and EU policies have presumed that collectively imposed vertical restrictions are harmful unless proved otherwise because of their deleterious effects on inter-brand rivalry. But vertical restrictions imposed by individual producers (except for Resale Price Maintenance) have received more favourable consideration (for a fuller discussion see Fishwick, 1993, pp.56-8). Following on from this logic, while the Act applies to vertical agreements, the government intends to exempt them via the Secretary of State's powers to make regulations. Therefore the prohibition in Chapter I will apply mainly to horizontal agreements (agree-

ments between potential competitors) rather than vertical agreements (agreements between firms at different levels of the supply chain; for a fuller review of the different forms of such agreements see Dobson and Waterson, 1996).

Based on a DTI consultative paper issued in September 1999, vertical agreements are likely to be excluded from the Act provided that there is no price fixing agreement and no 'complex monopoly' or market dominance which could adversely impact on competition (OFT, 1999e, para. 6.4). This means that particular terms found in vertical agreements, such as exclusive purchasing or distribution, tying provisions and obligations to take supplies of other products ('full-line forcing' agreements), are unlikely to fall within the terms of the prohibition unless there is price fixing or market dominance. By contrast, territorial exclusivity agreements can be expected to fall within the new Act, as will vertical agreements involving complex monopolies. In practice, however, there may very well be difficulty in providing a suitable definition of the criteria that leads to exclusion so as to remove all uncertainty for businesses. This reflects the uncertainty about the extent to which vertical restraints damage competition and are contrary to the public interest.

The Chapter I prohibition is intended to apply to all agreements from 1 March 2000. Agreements made before 9 November 1998 will still be considered under the terms of the 1976 Restrictive Practices Act until 1 March 2000. Agreements previously rendered void remain so; while agreements held to be previously outside the 1976 Act because of a lack of anti-competitive effect remain valid. There is a further transitional year beyond March 2000 for agreements that were not registrable under the 1976 Act. For agreements made between 9 November 1998 and 1 March 2000 special terms apply.

4. Regulation of Market Dominance

The 1998 Competition Act introduces a second prohibition (Chapter II, sections 17-24) relating to business conduct that leads to abuse of a dominant position in the market place. The market place is defined as any part of the UK and dominance will be taken to mean, following EU case law, the ability to act independently of competitors and customers (OFT, 1999f).¹⁶

Under the previous régime there was no prohibition on particular business conduct or a presumption that particular conduct was per se unlawful. Section 84 of the 1973 Fair Trading Act contains the public interest test and sets out illustrative criteria, but the approach is permissive rather than definitive. In their monopoly and merger inquiries Members of the MMC were required to take account of 'all matters which appear to them in the particular circumstances to be relevant', although the Act specified five elements to which they shall have particular regard namely '(a) of maintaining and promoting effective competition between persons supplying goods and services in the United Kingdom; (b) of promoting the interests of consumers, purchasers and other users of goods and services in the United Kingdom with respect of the prices charged for them and in respect of their quality and the variety of the goods and services supplied; (c) of promoting through competition, the reduction of costs and the development and use of new techniques and new products, and of facilitating the entry of new competitors into existing markets; (d) of maintaining and promoting the balanced distribution of industry and employment in the United Kingdom; and (e) of maintaining and promoting activity in markets outside the United Kingdom on the part of producers of goods, and of suppliers of goods and services, in the United Kingdom.' In practice the MMC has made infrequent direct reference to the criteria, though the criteria remain influential.

Under the 1973 Fair Trading Act, a legislative monopoly could be deemed to exist where at least

25 per cent of the share of supply of particular goods and services was controlled by one firm (a 'scale monopoly') or by a group of firms acting together by agreement or not so that their conduct prevents, restricts or distorts competition (a 'complex monopoly'). In all cases, in the first instance it was for the DGFT to determine the market so as to decide whether the undertaking or undertakings involved had a share of supply of at least 25 per cent and therefore fell within the statutory definition of a monopoly. The DGFT could then refer the firm(s) to the MMC for a monopoly inquiry where he felt that there was a prima facie case of anti-competitive behaviour.

Section 18(1) of the Competition Act provides an alternative framework by introducing a prohibition (the 'Chapter II prohibition') on 'any conduct on the part of one or more undertakings which amounts to the abuse of a dominant position in a market if it may affect trade within the United Kingdom'. The prohibition applies unless the matter is specifically excluded under the Act or subsequently excluded by an order issued by the Secretary of State. Identical to the terms of Article 82 of the EC Treaty, a 'dominant position' is not defined nor is 'abuse', but some specific examples are given. Borrowing directly from Article 82, Section 18(2) of the Competition Act provides the following guide:

Conduct may, in particular, constitute such an abuse if it consists in -

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

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

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature

or according to commercial usage, have no connection with the subject of the contracts.

While the examples under 'b', 'c' and 'd' are reasonably specific, 'a' is a catchall and the word 'unfair' is left for interpretation by the competition authorities and the courts.

Previously, while the OFT usually did undertake such a test, there was no legal prior requirement on the competition authorities to establish market dominance. Now the DGFT will be expected to review a market (by product or geography) and establish first that dominance occurs. This will be done by reference to market share, market structure, entry barrier and any other criteria that might be reasonably used in establishing market dominance (OFT, 1999f,g&h). Only once dominance is established will attention turn to whether the conduct by the dominant firm is illegal and this depends on the existence of 'abuse'. Once an 'abuse' of a dominant position is established, it will be prohibited subject to an appeal to the Appeal Tribunal.

Under the draft guidelines issued by the DGFT, following passage of the Act, conduct amounting to abuse will be divided into 'exploitive' and 'exclusionary'. Exploitive conduct includes the charging of excessive prices and price discrimination. Exclusionary includes predatory behaviour aimed at excluding competitors from the market, such as pricing below average variable cost, and certain types of vertical restraint that prevent a customer dealing with the supplier's competitors, provided a dominant firm is involved (otherwise it is likely to be outside the scope of the Chapter II prohibition and will be considered, if at all, under Chapter I). Also under draft guidelines the DGFT has suggested that an undertaking with a market share of less than 25 per cent will not normally be considered dominant; whereas one with a market share of over 40 per cent may well be dominant (OFT, 1999f). This revises the 'market share' criterion for a statutory monopoly from 25 per cent, that remains relevant to inquiries under

the 1973 FTA, to two thresholds of 25 per cent and 40 per cent. Some uncertainty remains, however, because the DGFT's definitions are simply guidelines and do not have force of law. They also provide for exceptions with the reference to 'normally'. The lack of precision reflects uncertainty in economics about the relation between market share, dominance and abuse. Measurement by market share may be misleading since power in a market depends, inter alia, on the market shares of other firms in the market, their competitive strategies, and on the potential competition in the market or the degree to which the market is 'contestable' (Baumol, Panzar and Willig, 1982).

What is clear is that as a result of the Competition Act various market share criteria now prevail in UK competition policy. The traditional 25 per cent threshold applies to monopoly investigations and merger enquiries¹⁸ under the 1973 Fair Trading Act (see below). The same percentage prevails when deciding whether an agreement under Chapter I should be regarded as infringing the prohibition (the 'small agreements' test). However, a 40 per cent market share held by one or more firms is the presumptive threshold for a finding of dominance under Chapter II, with some uncertainty for market shares of between 25 and 40 per cent. Moreover, in all cases other factors can be taken into account. The DGFT has already issued two formal consultation drafts, one on market definition and the other on the assessment of market power (OFT, 1999f&i). Both confirm that market share figures will not be taken as conclusive and there may be infringements of the Chapter I and Chapter II prohibitions at lower market shares than those stated. At the same time the DGFT has confirmed that a high market share is not of itself sufficient to be unlawful (*European Law Monitor*, February 1999, p.4). This is consistent with the need for 'abuse' to occur.

Although the Act has gone some way to aligning UK and EU competition law on market dominance,¹⁹ it is important to recognise that some differences still remain and that these extend beyond

considerations of market share. Some have already been referred to, for example relating to the levying of penalties. One particular area of further difference relates to market dominance.²⁰ Under EU law a dominant position is not prohibited only the abuse of dominance is illegal. Therefore conduct is prohibited and penalised only if it is the result of dominance. In other words, firms have been penalised under EU competition law for conduct that they could have pursued with impunity if they had not enjoyed a dominant position. Also, at the EU level it seems that conduct which strengthens a dominant firm's position is open to attack (the decisions of the European Court of Justice in the case of Continental Can in 1973 and Michelin Nederland in 1983 are good examples of this). By contrast, the MMC has not attacked dominance *per se* but rather monopolies that conflict with the public interest defined in terms of conduct and performance. Following the new Act UK competition policy still provides for control of 'anti-competitive' practices even in the absence of dominance, on the grounds that it may be that some of the undesirable consequences of oligopoly could not be controlled if it was always necessary for dominance to be established first. Oligopolistic, including duopolistic markets may be subject to collective market power because of the structural conditions in the market even though no one firm is dominant. Using powers under the 1973 Fair Trading Act, the Commission will still be able to continue to review market structures including scale monopolies and complex monopolies where requested to do so by the Secretary of State, on advice from the DGFT. Moreover, the OFT will be able to continue to mount a broad industry-wide inquiry (such as into new car sales) rather than one aimed at a particular undertaking or group of undertakings.

From a UK perspective EU policies have not been applied effectively to oligopoly problems. The European Court of Justice has been reluctant to accept application of a 'dominant position'

under Article 82 to groups of undertakings not financially or otherwise structurally linked and because of problems of distinguishing between the effects of 'tacit collusion' (or 'concerted practices') and of non-collusive 'parallel conduct' in oligopoly markets. An earlier DTI Green Paper (1992) pointed out that Article 86 (now Article 82) seems inapplicable to non-collusive oligopoly. This means that certain adverse effects of dominance of a market by a small number of firms - in the form of, for example, price leadership, excessive advertising or brand proliferation - may fall outside the scope of EU competition law when no agreement exists. It was for this reason that, in April 1993, the Government ruled out modifying UK law to bring it into conformity with Article 86 (now Article 82). The complex monopoly provisions that have been retained will capture parallel behaviour by a group of undertakings that appears to be anti-competitive but where there is no evidence of collusion or an agreement (if there was such evidence then potentially there would be a Chapter I infringement). The retained scale monopoly provisions of the Fair Trading Act are generally intended to deal with situations where there has already been a proven infringement of the Competition Act, but where the DGFT believes that there is a real prospect of further abuse (OFT, 1999h, para.13). The structural remedies available under the scale monopoly powers may be the only effective means of preventing further abuses (the scope is wider, however, in the case of the utility sectors, as discussed below).

Although the MMC and EU Commission (DG IV) approaches to monopoly or dominance have been similar - neither has adopted a *per se* approach to outlawing monopolies - UK policy has provided for control of the adverse effects of oligopoly and of anti-competitive conduct by individual firms without necessary proof of dominance or collusion. Lack of such a control is arguably a gap in EU policy. Although the prohibitions under the Competition Act tackle agree-

ments and concerted practices and abuse of a dominant position, they do not readily deal with parallel behaviour by parties where there is not an agreement. Therefore, the 'complex monopoly' provisions of the 1973 Fair Trading Act have been retained to regulate this kind of activity. In general, therefore, UK competition policy retains an attention to oligopoly or structural issues that may be unrelated to the abuse of dominance (Hay, 1998, p.29).

Finally, the Competition Act has not altered policy on the regulation of mergers. From an economic perspective competition policy should be concerned with the maximisation of consumer and producer surplus (in the short and long-run), but on the face of it EU merger regulation does not necessarily reflect this. If a merger 'creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or a significant part of it'²¹ it is prohibited, otherwise it is allowed. Under EU merger law there is not an efficiency defence as in the UK (and in France, Germany, the USA and many other countries).²² In the UK, wider public interest concerns can be taken into consideration when judging a merger. In the EU the only criterion is competition. Ironically, it was mainly the UK that imposed this limited scope during the negotiations that led to the EU policy in 1989. The UK feared that the European Commission might use wider public interest criteria to pursue industrial policy within Europe.²³

In summary, the new régime recognises that an approach to competition based simply on the Chapter I and II prohibitions is not appropriate and the public interest inquiry format into structural issues remains. This applies particularly in the fields of scale and complex monopolies and mergers.

5. Competition Policy and Utility Regulation²⁴

Privatisation in the 1980s and 1990s of British Telecom, British Gas, the water and sewerage and

electricity industries, and the railways led to the establishment of dedicated regulatory offices headed by their own director generals. The offices were modelled on the OFT but with each office undertaking specific regulatory functions relevant to their sector. Under the new Competition Act the director generals of these regulatory bodies, namely OFTEL, OFWAT, OFGEM and the ORR,²⁵ will exercise concurrent powers with the DGFT in the enforcement of the Chapter I and II prohibitions within their specific sectors. Previously the sector regulators had powers to refer certain scale monopoly and anti-competitive practices to the MMC. Now they have been given the same powers as the DGFT within their sectors to obtain information, investigate anti-competitive behaviour and the same duty to provide a reasoned decision (Section 54 and Schedule 10). The regulators also have concurrent powers with the DGFT to levy penalties on the companies they regulate for Chapter I and Chapter II breaches (OFT, 1999j).

The sector regulators also retain powers to negotiate and enforce companies' operating licences within the industries.²⁶ Where the regulator proposes licence changes that are disputed by the company then previously the matter was reviewed by the MMC. The issue referred was whether the existing state of affairs in the absence of the licence modification would be expected to operate against the public interest. If the MMC found that an adverse effect on the public interest could be remedied or prevented by a licence modification, the regulator made the final licence revision. Following the Competition Act the procedure is essentially unchanged, except that henceforth the review will be undertaken by panels from the 'reporting side' of the CC.²⁷

The Competition Act has extensively enhanced the powers of the industry regulators to police anti-competitive activities. At the same time, because of the difficulty of establishing competition in parts of the utility sectors, the full use of the scale monopoly provisions in the Fair Trading

Act is retained. This means that, unlike in the case of the other sectors of the economy, the scale monopoly provisions may be used whether or not there has been a prior infringement of the Competition Act (OFT, 1999h).

The regulated sectors include some of the most obvious examples of market dominance, therefore it is to be expected that some of the most interesting challenges under the new Act will arise here. A particular area open to challenge is the continued monopolisation of networks by companies.²⁸ For example, OFWAT (the Office of Water Services) and the OFT have already published a joint consultation document on the application of the Competition Act to the water sector (OFT, 1999k). Of all of the regulated sectors the water industry has remained the least affected by competition since privatisation, with each of the water companies continuing to possess almost complete market dominance. So far experiments to introduce competition, such as inset appointments, have been largely ineffective. As long as the incumbent water companies monopolise the means of delivery of water and sewerage services (pipelines, treatment plants etc) it is difficult to see how competition can progress far (Board, Boulding, Parker and Vass, 1999).

The joint consultation document signals how the powers in the Competition Act may be used by the regulator to introduce more effective competition. In particular, the document discusses the possibility of enforcing access to essential capital facilities on reasonable terms unless a refusal can be justified. That is to say, any refusal by a utility of access by another, potential supplier to an 'essential facility' in the service delivery may constitute an abuse (OFT, 1999g, para.4.49). The joint consultation document also suggests that undertakings that refuse to outsource contestable services may find themselves accused of abusing their dominance as purchasers in the market. In addition, long-term supply arrangements may be open to challenge if they preclude competition. The Competition Act (Schedule 3), in line with

Article 90(2) of the EC Treaty, provides for an exclusion from the Chapter I and II prohibitions where (a) an undertaking has either been entrusted with a service of 'general economic interest' or is a 'revenue-producing monopoly' (i.e. an undertaking granted monopoly powers by the state to raise money for the state); and (b) insofar as the application of the prohibition in the Act would obstruct the performance of the particular task assigned to the undertaking. The DGFT and the industry regulators will be required to apply these principles, which will be subject to ongoing interpretation. Nevertheless, they are unlikely to provide major protection to the UK utilities where government and regulators are keen to extend competition and profits earned belong to the shareholders not the state. The OFT/OFWAT paper underlines the extent to which dominant companies in the regulated sectors may find their activities open to challenge. Draft guidelines issued by the Office of Telecommunications convey a similar message to the telecommunications sector (OFTEL, 1999).

The result of the new competition régime is likely, therefore, to be considerable restructuring in the regulated sectors to avoid the Chapters I and II prohibitions. Moreover, the Act and existing regulation will combine to attack 'excess' profit making, as evidenced since privatisation (for figures and an analysis see Parker, 1999). The OFT has indicated that profits consistently exceeding a company's cost of capital may be taken to indicate that prices are excessive (OFT, 1999g, para.4.8). This will provide further ammunition for regulators to put pressure on utility companies with high rates of return to cut their prices, even before their price caps are adjusted at the next periodic review.²⁹ In other words, once the Act takes effect the regulators will be able to use both licence amendments and the Competition Act to control prices that are not competitive and deal with anti-competitive behaviour in areas that are potentially competitive, including prizing open access to monopoly

networks. At the present time the telecoms regulator is expected to make most use of the Competition Act to police markets because competition is most developed in this sector. It is to be expected, however, that as moves towards competition increase in the other regulated sectors there will be more recourse by all of the regulators to their powers under the Act.

Given that the Act confers concurrent powers on the regulators and the DGFT it would be possible for a company to be investigated for the same action by both the regulatory office and the DGFT. Following meetings between the regulators and the OFT, however, a code of practice has been established to avoid duplication. Normally the terms of the Act will be applied by the sector regulators rather than the DGFT.³⁰

6. Conclusions

The 1998 Competition Act is the most important piece of legislation affecting UK competition policy since the 1948 Monopoly and Restrictive Practices (Inquiry and Control) Act that established the Monopolies and Mergers Commission. From March 2000 prohibitions will apply relating both to restrictive practices and the abuse of market dominance. This brings UK competition policy more into line with EU law; although some important distinctions still remain particularly relating to structural issues, including the regulation of scale and complex monopolies, regulation of mergers and the precise penalties that may be levied. Powers under the 1973 Fair Trading Act have been retained that enable investigations into oligopolies independent of dominance issues and scale monopolies where the DGFT fears continued abuse; while mergers may still be considered in the UK using wider public interest criteria than is open to the competition authorities in Brussels.³¹

Economists are concerned with economic efficiency in which competition is simply a means to an end and monopolies are not per se undesirable (Vickers and Hay, 1987). Traditionally competi-

tion policy in the UK has recognised that large firms may benefit from economies of scale leading to static and dynamic efficiency gains, for example through higher R&D expenditures and 'synergies'. This approach to dominance continues within UK competition policy following passage of the Competition Act and dominance and mergers that increase market power are not automatically condemned. As in EU law, on which the Chapter II prohibition is modelled, it is abuse of dominance rather than dominance as such that is outlawed. The Competition Act has introduced a much more stringent approach to restrictive practices, however, where anti-competitive behaviour is usually the rationale. The Chapter I prohibition is a considerable change on the previous approach to regulating restrictive practices. It establishes a much tougher regime and one in which penalties for infringement are intended to be draconian.

The legislation has replaced the Monopolies and Mergers Commission with a Competition Commission and substantially enhanced the investigation powers of the DGFT. The 'reporting side' of the new Commission incorporates the previous inquiry functions of the MMC and a new Appeal Tribunal has been added to hear appeals against decisions of the DGFT and the sector regulators, including the penalties levied. Turning to the OFT, the DGFT now has extensive powers to investigate and levy penalties for anti-competitive behaviour. Obstructing the DGFT's enquiries or falsifying statements may lead to a prison sentence. The Competition Act has also introduced important changes to the regulation of the privatised utilities by giving the sector regulators concurrent powers with the DGFT over competition matters relating to their specific industries, namely telecommunications, gas, water and sewerage, electricity and the railways. As these sectors include some of the markets with the highest levels of dominance by one firm, it is to be expected that the Competition Act will have considerable implications for structure and conduct in these industries.

As a result of the Act customers and other businesses should now be better protected from undertakings which seek to rig the market to their own advantage. In addition to penalties levied by the DGFT or the industry regulators, for the first time it appears from parliamentary debates during the passage of the Act that government anticipates injured parties possibly mounting US-style anti-trust actions for damages in the courts. By giving the DGFT teeth - the powers to search and the powers to fine - plus the scope for third parties to take civil action, the result should be much greater incentives for businesses to comply with UK competition law than was the case in the past. One consequence is the need for organisations to establish formal corporate compliance programmes to ensure that infringements including accidental infringements of the legislation do not occur. It remains to be seen, however, how quickly firms accommodate themselves to the new prohibitions and reconfigure their behaviour to minimise the threat of penalties and civil actions. In this respect the results of a recent poll for the OFT, which found that more than 75 per cent of company chiefs appeared to be unaware of the powers in the Act, is illuminating (*Financial Times*, 1999).

In addition to tightening the law on anti-competitive behaviour, the intention has been to create a competition law that is more predictable in its effects for both consumers and producers.³² Some continuing uncertainty, however, is inevitable in what remains an effects-based competition policy. The precise consequences of the Act will be affected by how the Act is implemented and administered; how well it dove-tails with EU law; and in particular how well the Appeal Tribunal functions. Under the Act a good deal of discretion in operating the legislation remains with the DGFT, the Secretary of State and the utility regulators. Moreover, although the courts have been instructed to interpret the Act wherever possible in the light of European Court decisions, there may be circumstances where particular concerns

in the UK mean that there is a departure from the European Commission's assessment. It does not follow, therefore, that there will be complete consistency between UK and EU competition policy.

Endnotes

1. Aston Business School, Aston University.
2. The author was an additional panel member of the Monopolies and Mergers Commission and is a specialist panel member of the new Competition Commission. This paper is written in a purely personal capacity, however, and should not in any way be taken to represent the views of the Commission or of any other of its members.
3. Under the Amsterdam Treaty, from 1 May 1999 Article 85 of the EC Treaty became Article 81 and Article 86 Article 82.
4. This leaves time for companies to comply with the terms of the Act (detailed below) and for the necessary rules and regulations under the Act to be drafted. Agreements and provisions made before the Act takes effect benefit from transitional provisions unless void under other legislation. The transitional period is usually one year from the date that the prohibition takes effect, although some agreements benefit from extended transitional relief.
5. Members and the commission chairman are appointed by the Secretary of State from industry, commerce, public service and academia on recommendation by the DTI. Appointments are for an initial period of three years.
6. The CC retains powers to seek a time extension from the Secretary of State where this is considered necessary to complete an inquiry. The 1973 Fair Trading Act permits a maximum period of six months for a merger inquiry. Recent practice has been for the period to be set initially at three months. Newspaper inquiries are normally completed within two months.
7. Under the terms of the Fair Trading Act 1973, which still apply, mergers and acquisitions may be referred to the Competition Commission where they involve assets of over £70m. or a market share of at least 25 per cent. Newspaper and water company mergers are subject to separate terms that involve automatic referral above different thresholds. The new Financial Services and Markets Bill includes provision for the DGFT to make references to the CC where he considers that the Financial Services Authority's rules may be anti-competitive. This additional role for the CC is not considered further in this paper.
8. This goal has not prevented the Secretary of State from over-ruling or amending the recommendations of the CC in three recent cases, namely the British Airways takeover of City Flyer, Trinity newspapers takeover of the Mirror Group, and the monopoly inquiry into the supply of raw milk in Great Britain. The Secretary of State also over-ruled the DGFT and referred the NTL-CWC merger to the CC in November 1999.
9. The Tribunal members are in the course of being appointed following press advertisement.
10. The Secretary of State has power to prescribe further types of decisions covered by the right of appeal. Only in the case of an appeal against a penalty charge is the effect of an infringement decision suspended pending the outcome of the appeal.
11. There is also scope for aggrieved parties to seek a 'judicial review' of the actions of the DGFT, the regulators and the CC including the Appeal Tribunal. Judicial reviews are concerned with the rationality, legality and procedural fairness and not with the substance of the case.
12. This is something of a grey area. Where a procedural error by the DGFT affects human rights under the 1998 Human Rights Act (HRA) an appeal may be possible. For example, if the DGFT fails to allow a party access to documents that are on his file this could infringe 'the rights of defence' and this might amount to such a serious matter that an appeal to the tribunal occurs (Butterworths, 1999). The HRA requires the courts to apply the Competition Act in a way that is compatible with the rights under the Act.
13. DGIV has imposed penalties of up to 4 to 5 per cent of turnover and it is to be expected that the DGFT

will similarly refrain from levying the maximum penalties except in the most extreme of cases. The OFT has made it clear that price fixing and abuse of market dominance may lead to fines at or near to the turnover ceiling. The penalties are detailed in OFT paper 423 (OFT, 1999c). It appears that the OFT's starting point for fines will be a penalty of up to 10 per cent of an undertaking's annual turnover, though the relevant turnover when calculating the penalty will be the market affected by the infringement (the DTI is currently working on regulations to define what is meant by 'turnover'). This levy is likely to be for each year an infringement has occurred with a maximum of three years taken into consideration. This is more draconian than the penalty levied by the European Commission, which is a maximum of 10 per cent of turnover in the financial year preceding the infringement. Penalties will be mitigated, in some cases completely, for companies that inform of illegal cartel agreements in which they are involved. This should act as a further disincentive to enter into restrictive practices because it introduces the possibility of a 'prisoner's dilemma' style of strategic behaviour by parties to an agreement, involving revealing the existence of the agreement to the competition authorities to escape penalty.

14. The Secretary of State can restrict powers under the Act where these are considered to conflict with international obligations or where there are 'exceptional and compelling reasons of public policy' (Maitland-Walker, 1999, p.52). Individual and block exemptions covering certain classes of agreement may be made by the Secretary of State on advice from the DGFT subject to Parliamentary approval. Also, agreements covered by EU exemptions are automatically exempt from the prohibition under the 1998 Act. In addition, the secretary of state has powers to exclude from the prohibitions land agreements and certain professional rules. Land has always been subject to special treatment under competition law, for example certain restrictive covenants may not be covered, although restrictions on land use that prevent or distort competition are expected to be included.

15. OFT 1999c and d. The draft guidelines are reviewed in the *European Law Monitor*, February 1999. The threshold differs from that used by the European Commission.

16. An undertaking is dominant if it can behave 'to an appreciable extent independently of its competitors and customers and ultimately of consumers' when making commercial decisions (Case 27/76 *United Brands v Commission* [1978] ECR 207, [1978] I CMCr 429).

17. This contrasts with EC law where a 50 per cent market share is presumed to give rise to dominance. The market share applies to conduct by one or more undertakings.

18. For mergers, the £70m. assets test remains as an alternative.

19. The competition laws of 14 of the 15 member states, the exception is Germany, are now modelled on Articles 81 and 82 with the most recent legislative changes in this direction occurring in the UK and the Netherlands (Zinmeister, Rikkers and Jones, 1999, p.279).

20. Another difference relates to the scope of the right of appeal. This is less generous than under EU competition law (see Butterworths, 1999).

21. Council Regulation (EEC) No.4064/89, Article 2(3).

22. The possible exception is a 'crisis cartel' under Article 81.

23. In August 1999 the government announced a review of merger policy including proposals to make competition the clear primary goal and involving a possible change in the roles of the DGFT and the CC (DTI, 1999). It is also at present the case that the differences between the EU and OFT practices can be more apparent than real when deciding on the merits of a merger. The point here, however, is that as matters now stand the legal powers are different.

24. Certain industrial and commercial sectors where there are special commercial regulations, e.g. the financial sector and broadcasting, are excluded from the prohibitions under the Competition Act. The following discussion is concerned with those sectors covered by the Act where there are specific sector regulators (the privatised utilities or network industries).

25. The separate regulatory offices for gas supply and electricity, OFGAS and OFFER, were recently merged to form the new Office of Gas and Electricity Markets (OFGEM).

26. In 1997 the DG of OFTEL had effectively anticipated the new powers by introducing condition 18A into BT's operating licence. With the new Competition Act this licence condition seems redundant. It remains unclear, however, whether the DG of OFTEL will choose to remove it. Condition 17 of BT's licence also provides powers to the DG in relation to undue discrimination and undue preference. Again these powers now seem to overlap with those encompassed in the Competition Act.

27. As before, in the cases of telecommunications, electricity and water and sewerage these are specialist panels. Curiously the gas and railway privatisations did not make provision for specialist panels for these sectors and reviews are undertaken by inquiry teams drawn from the reporting panel of Commission Members. A specialist panel also exists for newspaper inquiries. Under the Utilities Bill to be introduced during the current parliamentary session, the regulatory offices will be required to confirm with the CC that licence modifications following CC reports adequately remedy the public-interest detriment found. This follows some uncertainty about the precise powers of the regulator following such a CC finding.

28. As a result the Act also may have implications for attracting private finance in the form of PFI/PPP schemes in areas such as transport, where local dominance of bus or rail markets results. Space precludes a more detailed discussion of this issue.

29. Under UK regulation companies are set price caps that are adjusted at periodic price reviews, usually held every five years.

30. Regulations are currently being drafted dealing with concurrency.

31. Although the recent government consultative document on mergers (DTI, 1999) proposed changes that would more align EU and UK merger policy any changes will require primary legislation, which is unlikely until after the next General Election.

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