

IN THE COMPETITION APPEAL TRIBUNAL

Case No: 1051/4/8/05

Hearing date: 13th December 2005

BETWEEN:

SOMERFIELD PLC

Applicant

and

THE COMPETITION COMMISSION

Respondent

SOMERFIELD'S SKELETON ARGUMENT

A. INTRODUCTION

1. In this skeleton, Somerfield addresses the following issues:
 - the standard of review to be applied by the Tribunal under section 120 – Part B;
 - the first issue under Ground 2 – the restriction on the identity of the stores to be divested – Part C;
 - the second issue under Ground 2 – the restriction on the identity of the permitted purchasers of those stores – Part D.
2. Ground 1 was withdrawn on 19th October 2005 and is not now in issue.¹

¹ Somerfield notes that the CC did not respond in its Defence to the President's invitation to address the background matters addressed in the President's remarks at the CMC on 1st November 2005 (Transcript 12/28-15/27). Somerfield will provide its comments as appropriate when the CC addresses those issues.

B. THE STANDARD OF REVIEW UNDER SECTION 120

NoA [19]-[24]; Defence [17-21]

3. The CC submits at paragraph 20 of its Defence that “the Tribunal, in reviewing the Competition Commission’s decision, must afford it [a] wide latitude or margin of appreciation” on the ground that it “is the public authority to which Parliament has afforded the power to remedy competition problems which domestic mergers may create”.
4. Somerfield submits that the normal standard of review applies, as set out in its NoA [19]-[24]. There is no reason for giving the CC a wider margin of appreciation than that afforded to the OFT under the Act or the European Commission under the EU Merger Control Regulation. Unlike the previous merger control regime under the Fair Trading Act 1973, there is no political accountability in Parliament for the decision which remedies to impose. The lack of a political check on the CC’s exercise of these powers justifies an intensive review by the Tribunal.
5. The CC’s divestment requirement is, in any event, an interference by a public body with the right to peaceful enjoyment of possessions. The burden is therefore on the CC to show that its decision is proportionate: see NoA, [21].

C. FIRST ISSUE: RESTRICTION ON IDENTITY OF STORES TO BE DIVESTED

NoA, [101]-[105]; Defence, [24]-[36]

Introduction

6. The CC misrepresents Somerfield’s case at paragraph 25 of the Defence. The CC states that Somerfield’s case is that it can never be reasonable or practicable for remedial action under sections 35 and 41 to preclude choice of divestment asset. That is not Somerfield’s case.
7. Somerfield acknowledged throughout that the CC was entitled to be satisfied that the store to be divested would be disposed of within a reasonable time frame and to a suitable purchaser.² This reflects the concerns laid down in paragraph 2.4 of the CC’s Guidelines on Application of Divestiture Remedies in Merger Enquiries as to “composition risks” (that the scope of the divestiture package may be too constrained or not appropriately configured to attract a

² See e.g. NoA/30/545/2.3 and NoA/33/586/3.34.

suitable purchaser) and "purchaser risks" (that a suitable purchaser is not available or that the merger parties will dispose to a weak or otherwise inappropriate purchaser). Somerfield also recognised throughout that where there was more than one existing (or "proximity") store, further consideration would be needed.³

8. Somerfield's contention is that the choice of divestment asset should, in the ordinary course and absent special factors deriving from the concerns outlined in the previous paragraph, be that of the owner who has a legitimate interest in determining which of the assets he wishes to retain. Somerfield submits that, in the circumstances of this case, the factual basis upon which the CC found SLC and the wide power it has to devise a suitable structure of the remedies "process and timetable" (the terms used in [11.23]), as illustrated by the remedies process devised in this case and especially for the locations in which it gave Somerfield the choice of divestment store [11.24-11.38], do not give the CC any basis upon which to preclude Somerfield from choosing whether to divest acquired or proximity stores in order to remedy the specific SLC that has been found.
9. The CC's remedies package requires Somerfield to dispose of relevant stores to eligible purchasers.⁴ During the initial stipulated period (its length is confidential and need not be referred to in open court), eligible purchasers are limited to the competitor set identified by the CC at Stage 1 (subject to the exclusions at Appendix G of the Report: see [11.29]) plus any other purchasers satisfying the CC that they would offer comparable PQRS (see [11.26]) and Somerfield may seek offers from those purchasers only. If, but only if, no interest is shown in that time by anyone within the restricted set of eligible purchasers, Somerfield may market more widely, including to LADs ([11.28]). If Somerfield fails to achieve divestment in the first divestiture period (the length of that period is also confidential and need not be referred to in

³ However, in practice, and as is recognised by the CC at paragraph 79 of Christopher Clarke's statement, the issue of multiple proximity stores did not determine its conclusions in any of the locations with which the Tribunal is concerned.

⁴ In the light of the bringing of these proceedings, discussion of the final undertakings was halted and the position is governed by interim undertakings as the Tribunal is aware.

open court), a divestiture trustee is then appointed and can dispose of the stores [C]⁵).

10. These arrangements differ from those adopted by the CC in the *Morrisons/Safeway* inquiry because, among other things, [C].
11. There is no reason why the divestiture trustee arrangements could not relate to either the acquired or a proximity store, which is exactly what the CC ordered in respect of the three locations where it gave Somerfield the choice⁶: [11.34]. Thus, the CC could have assured itself that in any event one or other store would be disposed of.
12. The CC's decision to specify that the acquired store should be divested (in seven cases: the four in which it rejected Somerfield's desire to divest an existing store⁷ and the three in which it ordered Somerfield to divest the acquired store⁸, albeit following Somerfield's expressed preference if put to the choice⁹) is therefore perverse and disproportionate and exceeds what the CC could reasonably have thought necessary to remedy the SLC that it had found.
13. Where the CC gave Somerfield the choice between divesting the acquired or an existing store, that is exactly what it should have done throughout.¹⁰

The CC's statutory powers

14. The starting point for the CC's remedial powers is that they may be exercised "for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned" (section 35(3)). In order to determine how that SLC is to be remedied, it is therefore crucial to identify how it has been found to arise. The SLC to be remedied does not exist in the abstract: it

⁵ NoA/40/1031, line 20 and 1032, lines 32-33. Somerfield reserves its position in respect of the CC's draft final undertakings. [C]

⁶ Namely, in respect of Johnstone, Peebles and Yarm: [11.19]-[11.21].

⁷ Namely, Middlesbrough Linthorpe, Newark, Pocklington and South Shields.

⁸ Namely, Filey, Poole Bearwood and Whitburn (Scotland).

⁹ Contrary to Christopher Clarke's assertion at sub-paragraph 46(1) of his statement, Somerfield's position here is not difficult to understand. It asked to be given the choice. Its alternative position was to specify in certain locations which store it would like to divest and the CC agreed with it in respect of those three locations. However, Somerfield maintained throughout and maintains now that it should have the choice.

¹⁰ Its agreement with Somerfield that the closed stores in Littlehampton and Kelso should be sold rather than the acquired store (sale of which would not alter the competitive position in those locations) calls for no further comment in these proceedings.

is the specific SLC concerned and the subject of the CC's report setting out its reasons in accordance with section 38.

15. In this case, the SLC identified by the CC arose because of the transfer into common ownership of stores previously under separate ownership in local grocery markets. That position is restored through separation of ownership of the stores: the identity of the grocery retailer owning each particular store after divestment cannot be relevant provided that that retailer will continue to provide a competitive constraint on the retained store (see further below in relation to the second issue). Separate ownership ensures a resumption of the process of rivalry.
16. Nor is it relevant whether the proximity store is smaller or exerts a weaker competitive constraint on the acquired store than the acquired store exerts on the proximity store. The competition issue has arisen because those two stores have come under common ownership; and the remedy, all other things being equal, is to ensure that they become once more separately owned.
17. If as a result Somerfield becomes the owner of the stronger store in an isochrone and divests itself of the weaker store, the *status quo ante* – stores in rival ownership – is restored. There is no reason in principle why an acquirer should not derive that benefit from the deal as competition is unaffected. By the same token, there can be no principled objection to Somerfield selecting a Kwik Save as the divestment store.¹¹
18. Somerfield was perfectly entitled to complete the deal unconditionally and without prior notification. If the final sentence of paragraph 32 of the Defence implies anything different, the criticism is misplaced. Certainly, the fact that this case concerns a completed acquisition and the *Morrisons/Safeway* report concerns a prospective acquisition is not a valid distinction between the two.
19. The fact that the CC should, from a competition perspective, be indifferent as to whether the acquired or an existing store is sold applies with particular force in the present case because the CC measured the SLC concerned on the basis that the competitive constraint offered by the existing store to the acquired store is equal to the one imposed by the acquired store on the existing store (the assumption of symmetry¹²). There is no other basis for the

¹¹ Contrast the view expressed in Christopher Clarke's statement at paragraph 30 .

¹² For the record, Somerfield contests Mr Davies's assertion in paragraph 24 that the symmetry assumption was needed for the illustrative price rises to be calculated: as

finding of SLC. That defines the SLC concerned in this case: under section 35(3) it must also define the remedy to that SLC. The confusion to which Mr Clarke and Mr Davies confess (paragraphs 96 and 20-32 of their respective statements) simply does not arise.

20. The CC [11.13] renounced symmetry when it came to remedies (“we do not therefore accept ... that there is necessarily symmetry between the divestment of either the acquired or the existing stores.”). It was wholly inconsistent and illogical of it to do so, having found the SLC concerned on this basis. Furthermore, the CC does apparently accept Somerfield’s point of principle that selling either the acquired or existing store will ordinarily remedy the SLC, the CC justifying its departure from this principle by reference to the matters at [11.12] of the Report.¹³

The CC’s Defence on remedy – saleability

21. The CC now states at paragraph 32 of the Defence that its key consideration in determining the remedy was “saleability” of existing stores. Somerfield observes at the outset that in circumstances where [C], the emphasis now placed in the Defence and by Mr Clarke on the importance of the consideration of saleability as a reason for not permitting Somerfield the choice of stores is surprising.
22. The Defence states that the CC decided that acquired stores must be sold in those areas where [C].¹⁴
23. In adopting this approach, the CC decided that there were good reasons to deviate from the initial approach adopted in *Morrisons/Safeway* ([11.11] to allow choice of stores in all cases. Here, the CC considered that the stores involved are almost all mid-range stores with a diverse range of characteristics whereas *Morrison/Safeway* was largely concerned with larger one-stop shops. A “key difference”¹⁵ is said to be the diversity of mid-range

Mr Ridyard points out at paragraphs 17 and 18 of his statement, the textbook that says that the formula used by the CC is useless if symmetry does not hold includes a variant of the formula to use in asymmetric conditions.

¹³ Christopher Clarke's statement, paragraph 55: “I accept that, where the considerations raised in paragraph 11.12 do not apply, Somerfield is correct in saying that selling either the acquired or existing store will remedy the SLC.”

¹⁴ Defence, paragraph 32; see also Christopher Clarke's statement, paragraph 71.

¹⁵ Christopher Clarke's statement, paragraph 24.

stores which can affect their "saleability" to a much greater extent than one stop-shops which in this respect are generally much more homogeneous.

24. Thus the CC states at [11.22] in respect of four locations (Middlesbrough Linthorpe, Newark, Pocklington and South Shields) its view that "divestment of the existing store would be significantly inferior to divestment of the acquired store in remedying the SLC as these [stores] have a significantly greater risk of not attracting a suitable purchaser able to offer comparable PQRS to that which was offered before the acquisition".
25. Mr Clarke confirms at paragraph 79 of his statement that two other considerations identified at [11.12] of the Report were not determinative of the CC's remedies conclusions, namely the potential need to reassess the identity of acceptable purchasers if the existing store is sold and the possibility that sale of an existing store may fail to remedy SLC where there is more than one existing store in the isochrone.
26. Somerfield submits that, for reasons outlined above, the CC had no basis under section 35(3) to make the determination that it did in the seven disputed cases in the circumstances of this case.
27. In any event, Somerfield submits that, properly considered, there was no evidence before the CC upon which it could properly reach the conclusion that it did as to "saleability". Apart from information provided by Morrisons as to which of the acquired stores had not been the subject of offers from other grocery retailers, the CC simply had and has no idea about the ease or difficulty of disposing of any of the stores in question other than that supplied by Somerfield. The CC did not seek evidence (for example from valuers or potential third party purchasers) as to the saleability of the stores in question or more generally in relation to the factors which affect the ability to sell stores. The only information it had as to saleability was supplied by Somerfield.¹⁶ The CC had no basis on which to disagree with Somerfield's assessment and cannot say that its assessment was that there was a "real risk" that any of the existing stores proposed for divestment would not sell.
28. What the CC actually did in its inquiry was to try to work out whether acquired and proximity stores were comparable (and therefore, no doubt, as a matter of intuition a broadly similar sale proposition). If they were comparable (as

¹⁶ See Somerfield's evidence at the Remedies Hearing, NoA/40/1030-1049 and subsequent submission, NoA/33/586, paragraphs 3.28-3.37.

the CC saw it), it gave Somerfield the choice (Johnstone, Peebles and Yarm); if not it either agreed with Somerfield that the acquired store should be sold or imposed that as a requirement (the seven cases in dispute).

29. The CC's conclusions at [11.22] of the Report are no more than an inference based upon a comparison of certain characteristics of each of the stores in question relating to:
- (i) financial performance;
 - (ii) size and physical condition; and
 - (iii) amount of car parking.
30. Unless those matters would deter any purchase by a grocery retailer, then they go only to consideration for the sale, not to saleability itself.¹⁷ In fact, the CC had sought no evidence and had none before it as to the effect those characteristics would have in practice on potential purchasers.
31. The ability to sell a store self-evidently depends upon a variety of factors, including the requirements of different purchasers and the consideration to be paid. While the CC correctly observes at paragraph 32 of the Defence that "not all stores are equally attractive to potential relevant buyers" this does not amount to anything more than an observation that each store has its own characteristics which are reflected in the consideration that a potential buyer is prepared to pay for the store.
32. The CC's focus on comparability rather than saleability can be seen from the CC's decision in relation to Johnstone, Peebles and Yarm where it concluded that Somerfield could choose which store to sell. This was on the basis that there was not much to choose between the acquired and the existing store (see [11.19] and [11.20]: "there is little material difference in the characteristics of the acquired and existing store"). But the CC's reason for giving Somerfield the choice seems to have been that because the respective stores were (in its view) very similar, disposal of either would remove the

¹⁷ Somerfield submits that the CC's "key difference" (see paragraph 23 above) is no "difference" at all. The CC did not consider such matters as relevant to saleability in its Report into *Morrisons/Safeway* (2003). The diversity among OSS as regards size – which can range from 15,000 to 50,000 sq ft or more (see NoA/33/585, paragraph 3.31) – is at least as great as among mid-range stores, and indisputably their condition can be as variable as that of mid-range stores. In addition, the diversity was not sufficient to persuade the CC to sub-delineate the mid-range into three separate sections as had been proposed by the OFT and was investigated and rejected by the CC at [6.64]–[6.65].

SLC; the CC does not refer to saleability in [11.20] at all. Thus, it appears that the CC's real concern was not with saleability but with establishing that, if an existing store was to be sold, it could be regarded as of broadly comparable competitive weight with the acquired store. That is an irrelevant consideration to which the CC should not have had regard. Its genesis can be seen in the approach of the various members of the inquiry group at the remedies hearing.¹⁸ It is an approach that may be explained by a general distrust of Somerfield's motives in its choice of store¹⁹ but that should not have swayed the CC's thinking.

33. Thus the CC did not have before it evidence as to the impact on saleability of the size or condition of a store, or its financial performance, or the extent of parking facilities available. Briefly on those issues, Somerfield makes the following observations. Relative size is not an obstacle to saleability: indeed, the CC has found that the larger retailers (Tesco, Sainsbury) are perhaps more likely to be interested in the smaller end of the convenience/mid-range segment.²⁰ Conversely, competitors such as Co-op are likely to be interested in the medium sized stores. Condition goes to price, not saleability. The same may be said for financial performance. Parking facilities may be less of a consideration for smaller stores, or those situated in high street or other locations where many customers will reach the store on foot.
34. Furthermore, the CC disregarded relevant evidence as to saleability provided by Somerfield, notably as to the relative ease of disposing of freehold properties as opposed to leasehold, especially where the remainder of the lease term is relatively short. Thus, in relation to **[C]** (see [11.16]), the CC has disregarded that aspect, which does go to saleability, and been swayed by its assessment of other factors such as size, condition and so on (see [11.22]), which in Somerfield's submission do not go to saleability.
35. However, in any event, if the approach taken to Johnstone, Peebles and Yarm had been followed in all cases, the structure of remedies would have been that if Somerfield failed to sell the existing store in the initial divestment

¹⁸ NoA/40/1033, lines 33-38; 1033b/3-17; 1038/31-32; 1043/19-26. See also the preparatory material received by the members of the group from the CC's staff in the exhibits to Christopher Clarke's statement CC/1/2 (page 16, para. 19); CC/1/3 (page 25, second bullet).

¹⁹ Christopher Clarke's statement, paragraph 19

²⁰ The CC refers at [6.17] and [6.22] to evidence it received that "some of the major grocery retailers have expanded into the convenience sector". See further [7.44] and Appendix F, in particular paragraphs 2 & 5.

period, the CC could have required divestment of acquired stores, ultimately [C].

36. Finally, in relation to Filey, Poole Bearwood and Whitburn (where Somerfield proposed divestiture of the acquired stores, in the alternative to its primary position that it should have the ability to choose the divestment store), if the Tribunal accepts Somerfield's submissions that the CC had no power to require Somerfield to divest particular stores, and the matter is remitted to the CC, there is no prejudice in permitting Somerfield the choice in relation to those stores that it should have had from the outset.

The other considerations not determinative of the CC's remedies conclusions

37. The two other considerations identified at [11.12] of the Report were not determinative of the CC's remedies conclusions. However, as these will need to be considered if the matter is remitted to the CC, Somerfield makes the following comments.

Sale of an existing store may fail to remedy SLC where there is more than one existing store in the isochrone

38. In Section I, paragraphs 6-17 of his statement, Mr Davies outlines a number of scenarios in which, if there are two proximity stores, the sale of either one of those stores might in theory not address the diversion ratio on which the CC has relied for its SLC conclusion. This part of Mr Davies' statement is unexceptionable, but it is largely of academic interest only.²¹ Only in relation to Middlesbrough Linthorpe does the situation on the ground in any way resemble the theoretical diagrams set out by Mr Davies at paragraphs 10-14 such that, if the CC's decision falls for reconsideration, Somerfield would accept that it would need to satisfy the CC that the proposed divestment would indeed reduce the diversion ratio. In the other situations of multiple proximity (Johnstone, Littlehampton and South Shields), the existing store proposed for divestment is sufficiently close to the acquired store to remove concern.

²¹ For completeness, it can be noted that the discussion of the scenario depicted in Figure 2 of Mr Davies' report is incomplete, since the impact that the sale of store 2 would have on competitive constraints on store 1 and the acquired store would depend on the constraints that arise outside of the isochrone Mr Davies has drawn.

Potential need to reassess the identity of potential purchasers if the existing store is sold

39. Somerfield believes that the CC has the necessary information to carry out this task should it be necessary as GeoBusiness would have details of stores and fascias within the isochrone centred on the existing stores, which was needed for the recentring analysis carried out at Stage 1.

Conclusion on the first issue

40. Accordingly, Somerfield submits that, on the basis of the Report, the CC had no power to require Somerfield to divest particular stores.

D. SECOND ISSUE: RESTRICTION ON PERMITTED PURCHASERS

NoA, [106]-[114]; Defence, [37]-[50]

Introduction

41. Somerfield's case, in essence, is that the exclusion of the LADs from the competitor set at stage 1 of the CC's analysis on an avowedly conservative basis does not mean that they should be excluded from the range of potential divestees.
42. First, having chosen to include or exclude operators in an approved competitor or divestee set on the basis of the competitive constraint that they offer to Somerfield (see [6.41]), it is wholly illogical for the CC then to differentiate between competitors on the basis of their business model or consumer proposition. Disposal to an operator with the requisite degree of competitive impact cannot be said by the CC not to remedy the perceived SLC.
43. Secondly, given the reduced importance of the "competitor set", as part of an avowedly conservative Stage 1 in a two stage process, within the CC's methodology for establishing SLC in certain local markets, the CC should not have equated membership of that competitor set as being the only effective criteria for classification as a suitable purchaser of any divestment store.
44. In response, the CC argues at paragraph 45 of the Defence that there are five pieces of evidence (including but not confined to the competitive impact assessment) referred to at paragraph 6.43 of the Report which were taken into account by the CC in deciding to exclude the LADs as potential divestees.

45. Somerfield submits that, properly considered, the CC could not reach the conclusion that it did on a balanced assessment of these pieces of evidence. There is only one serious piece of quantitative evidence and that is the competitor impact assessment. The remainder are weak, devoid of real content and/or inconclusive for reasons given below and it was perverse of the CC, if that is what is being said, to attach more weight to them collectively than to the competitor impact assessment.

46. Somerfield's submissions in response to the evidence to which the CC points are set out following the same order as in the CC's Defence.

(i) the range and nature of products offered by the LADs

47. At paragraph 47 of the Defence, the CC does not (and it could not) dispute Somerfield's evidence (see NoA [113]) that the LADs offer a range of products which, even if limited, nevertheless represents a large proportion of total grocery sales. *Prima facie*, this demonstrates the potential for significant competitive impact and therefore suggests that the CC was wrong to exclude the LADs from the range of permitted divestees for this reason. It is surprising that the CC did not even refer to this evidence in the Report.

48. Moreover, there is a broader point here that should affect how this piece of evidence is evaluated against the actual evidence on competition between the different fascias. The CC accepts that retailers compete across the spectrum of PQRS. Range, "R", is one facet of that competition. The relative breadth of the product range is no more than a simple descriptive fact. The real question is the relevance of that fact to the assessment of whether the LADs can provide a constraint to Somerfield. When it comes to assessing the evidence on such impact, the narrower product range of the LADs is already factored into the competitive impact assessment. To the extent that a narrow range diminishes the impact that a LAD can have on Somerfield (because in theory some of the Somerfield turnover, relating to items that the LADs do not stock, is "immune" from competition from the LADs) the impact of that supposed handicap should itself be picked up in the empirical evidence on impact. Thus, the facts regarding the more limited range of the LADs is not, as the CC appears to suggest, an additional piece of evidence that deserves separate attention, but rather is a piece of evidence that is already subsumed in the empirical evidence that is used to test the competitive constraints in practice.

(ii) the competitive impact assessment

49. The competitive impact statement is at Appendix B of the Report (NoA/1/ B1). Somerfield accepts that this is a properly executed and systematic analysis of data supplied by Somerfield as to the impact on sales at its Somerfield and Kwik Save stores of the opening of various competitor fascias.²²
50. Somerfield submits that the competitive impact assessment, as Mr Ridyard explained, demonstrates the inconsistency of the CC's approach to LADs compared to its approach to [C] and [C]: "The CC's evidence of competitor impacts showed that these retailers [i.e. [C] and [C]] exerted a competitive constraint on Somerfield that was significantly less than that exerted by Tesco, yet the CC chose to include them in the competitive set when it came to possible buyers of the divestment stores". This is a clear inconsistency in treatment because the "the LADs are shown by the CC's analysis to exert a similar constraint" on Somerfield to that of [C] and [C].²³ Indeed, the CC stated that "Somerfield pointed out that under our competitive impact assessment, the impact of a new [C] opening was similar to that of [C]. This we accept." ([6.43])²⁴
51. The findings of the competitive impact assessment are illustrated by Figure 1 in Appendix B²⁵ which shows the LADs alongside [C] and [C] in relation to their impact as competitors on Somerfield. Figures 2 and 3 in that Appendix

²² As Somerfield told the CC at the second hearing: see the comments of Mr Ridyard: NoA/39/870-871, lines 37-40.

²³ Ridyard, paragraph 87: NoA/2/26. On the issue of the significance of the constraint, Christopher Clarke, at [112] demonstrates the confusion into which the CC has fallen. He states that the quantitative evidence "tended to confirm our initial view based on product range and nature of their products that the LADs did not exert a significant degree of competitive constraint on Somerfield stores." This is wrong. The CC results show that the LADs' effect is significantly smaller than that exerted by Tesco, but not that it is insignificant. If the impact analysis had shown that LADs had an insignificant effect, Somerfield's argument would be lost. In fact, their impact is as significant as that of other operators included in the competitor set.

²⁴ Mr Davies asserts at paragraph 33 of his statement that Mr Ridyard "appears to suggest" that the CC should have done a full SSNIP test. Mr Ridyard made no such suggestion. He simply said at paragraph 84(ii) of his statement, NoA/2/25, that just because a full SSNIP test is not possible, it is not valid for the CC to act in a way which is inconsistent with the SSNIP test principle that the candidates for market definition should start from the narrowest set of products and work outwards. By excluding the LADs and including fascias that are no closer as rivals, the CC violated this simple and fundamental principle, and acted inconsistently.

²⁵ NoA/1/B3.

show this when the LADs are measured against the benchmarks of Tesco (Figure 2) and Asda (Figure 3).²⁶

52. The CC's case in relation to the competitive impact assessment is set out by Mr Davies at paragraphs 75-82. Mr Davies chooses to disregard the evidence in relation to Netto completely and to rely upon what he describes as the "actual average impact of [C] and [C] openings on Somerfield stores" which he asserts is "substantially higher than ... [C] and [C]" (paragraph 80). He concludes at paragraph 82 that the data shows that "[C] would appear to impose a greater level of competitive constraint than [C] and [C]". However, Mr Davies's analysis is seriously flawed and does not support the conclusion he seeks to draw.
53. Mr Davies asserts at paragraph 77 that data in relation to Netto can be disregarded. It is one thing to say that the Netto impact, being based on just one single observation, is on its own insufficient to form the basis for a robust conclusion. It is quite another, however, to say that as a consequence that observation should be discarded from the assessment altogether. Indeed it is thoroughly bad practice to discard valid observations from a statistical exercise. As Mr Davies clearly realises, such evidence as there is in relation to Netto supports Somerfield's case, not that of the CC.
54. Moreover, Mr Davies' decision to discard this valid (if inconvenient) observation is all the more surprising in view of the fact that in his own statement he demonstrates a valid way to incorporate the Netto observation into the analysis at several points.
 - (i) Paragraph 44: Mr Davies states as follows: "the product offering and business model of each of the LADs is similar, while at the same time being significantly different from those of the main supermarket operators within the competitor set. The Group therefore took the view that it would treat the LADs in the same way unless there was good evidence that different conclusions were warranted."
 - (ii) Paragraph 46: Mr Davies comments approvingly on the fact that Somerfield "focussed on the status of the LADs as a group, rather than the three LADs individually".

²⁶

NoA/1/B8-9.

- (iii) Paragraph 65: Mr Davies cites the “average diversion ratio to the LADs”, thus clearly aggregating their evidence in a single summary statistic.
 - (iv) Paragraph 68 (in relation to his discussion of the NOP survey): Mr Davies comments on the Group’s conclusion that “*the LADs as a group* exerted a level of competitive constraint materially below that of the main supermarket operators” [emphasis added].
55. In short, there appears to be absolutely no disagreement between Somerfield and the CC as to the validity of analysing the LADs as a group. Accordingly, it is obvious that the competitive impact of the LADs ought to have been considered collectively, and the Netto data included in that analysis. Yet inexplicably Mr Davies has chosen to keep the individual LADs separate in his discussion of the impact analysis, and has in effect simply thrown away the observation that relates to the competitive impact of the Netto opening.
56. Mr Davies’s table at paragraph 80 purporting to demonstrate the “actual average impact “ of openings is based on data which has not been adjusted for either the size of store concerned or the distance of that store from the Somerfield stores (or for any other matter). Obviously, both store size and distance (along with other factors) affect competitive impact, as the competitive impact assessment correctly explains at Appendix B, paragraph 13.²⁷ The whole point of the competitor impact analysis is indeed to control systematically for such factors.
57. This becomes particularly important when one considers that in the data set examined by the CC, the Aldi and Lidl stores are, on average, smaller than the Co-op and Waitrose stores and on average they are further away from Somerfield stores than Co-op and Waitrose stores. Accordingly, a failure to adjust the data to take account of different store sizes and distances will lead to a simple average being highly misleading. It is therefore wrong for Mr Davies, and inconsistent with the CC’s position at Appendix B, to place any weight on the unadjusted data in the table at paragraph 80 as he seeks to do at paragraph 82 (“That conclusion is even stronger in respect of the unadjusted data”). This is particularly egregious since the CC has done the work that is designed specifically to control for these very biases.

²⁷ NoA/1/B4.

58. Mr Davies' table at paragraph 81 is, by contrast, based on adjusted data, taking into account store size and distance, although still wrongly excluding the data for Netto. By contrast with the table at paragraph 80, it shows a much lower divergence in average impact between [C] and [C] on the one hand and [C] and [C] on the other. Of course, the question that any statistician would naturally ask is whether the differences that emerge between the LADs and the other fascias are statistically significant. This point is well understood by Mr Davies at paragraph 59 of his statement where (in relation to the NOP survey) he specifically refers to whether the differences that emerge in that work as between the LADs (note "as a group", not individually) is statistically significant. Oddly, however, when it comes to the description of the impact study Mr Davies omits to explain that the difference between these figures is not statistically significant.²⁸ This is, however, clearly set out in the competitive impact assessment at Appendix B: see paragraphs 9 and 24-27.
59. In addition, Mr Davies's analysis concentrates only on the Somerfield impact analysis and ignores these for Kwik Save where it is shown that [C] has a greater relative impact than both [C] and [C], [C] has a greater relative impact than [C] and is comparable to that of [C]. In many of the SLC isochrones, the existing stores are Kwik Save so in determining to whom the divestment store is to be sold, the CC needs to take into consideration the different competitive impacts of Kwik Save and Somerfield.
60. In summary, the Tribunal ought to take no account of the figures in either of the tables at paragraphs 80-81 of Mr Davies' statement. By the CC's own admission, neither table provides any, or any statistically significant, basis for drawing a distinction between the likely competitive impact on Somerfield of stores owned by [C] (and on Kwik Save of stores owned by [C] and [C]) on the one hand and [C] and [C] on the other. Mr Davies is making an invalid attempt to draw attention away from what is in fact a rather plain and obvious conclusion to be drawn from Appendix B, namely that there is no basis by reference to their ability to compete with Somerfield to exclude the LADs from the range of potential divestees.²⁹ Somerfield's position on this point is that the one exercise, carried out by the CC itself, which attempts systematically to

²⁸ Contrast paragraph 59 of his statement where he recognises the importance of statistical significance.

²⁹ Mr Davies's conclusion at paragraph 86 of his statement that Somerfield's case has ignored "all the evidence except for one data point in one piece of analysis" is simply wrong.

measure the impact of different fascias on Somerfield, strongly supports Somerfield's case.

(iii) the views of supermarket operators as to their perceived competitors

61. The views of supermarket operators are obviously to be treated with considerable caution as they each have good reason to answer such a question strategically. They are not a sound basis upon which the CC could proceed. However, the Report itself notes at [6.44] that at least Tesco regards the LADs as competitors, and that Mid-Range operators (including Somerfield) consider the LADs as offering a high level of perceived competition.³⁰
62. The approach taken is also inconsistent with the CC's correct recognition that OSS operators may not see themselves as constrained by mid-range operators but the reverse will not be true. That would explain why OSS operators might ignore or disregard competition from LADs, and also why OSS operators would not be best placed to comment on the subject of competition posed by LADs.
63. As to the views expressed by LADs that they did not consider Somerfield to be a competitor, referred to by Mr Clarke at paragraph 117 of his statement, that is irrelevant, as is clear from the next paragraph of his statement: the question is whether the LADs act as a competitive constraint on Somerfield.

(iv) the NOP survey results

64. The CC rightly acknowledges that "one should be wary of placing too much weight on the NOP survey results" (Davies, paragraph 62). Somerfield submits that in fact no weight can be placed upon the survey because it was not designed for and is unsuited to the purpose for which it is relied upon at paragraph 6.43 of the Report.³¹ (It should be added that although Somerfield was consulted as to the design and content of the survey, it can hardly be expected to have guessed that it would be used for this purpose.)
65. The fundamental flaw in the use of NOP survey for this purpose is that the results are not adjusted for matters such as store size and distance. As has already been explained, there are fewer LADs than other stores in the areas

³⁰ Appendix C, Table 2: NoA/1/C2.

³¹ Mr Davies's reference at paragraph 57 to sample sizes for political polls ignores the fact that those polls have properly weighted samples, and most certainly do not rely on the "next person available" approach taken by NOP in this survey – see NoA [57].

surveyed (nationally, Tesco has more stores than all the LADs put together) and thus on average, there are fewer of them close to a surveyed store. Accordingly, when the “next person available” was asked where s/he would have shopped had the store s/he had just left not been available, it is unsurprising that on average the answer was less likely to be diversion to a LAD rather than another closer fascia. However, this answer gives no information at all as to whether a store of a given size and proximity owned by a LAD would offer a significantly different competitive constraint to Somerfield from that offered by an equivalent store owned by another grocery retailer.

66. Thus Mr Davies’s conclusion at paragraph 59 that the difference between the customer diversion ratios to LADs and to **[C]** was “statistically significant” is completely undermined by his failure to take into account the fact that there are more **[C]** than LADs (indeed at a number of locations in the survey there are multiple **[C]** stores³²), making it more likely that there would be diversion to a **[C]** rather than a LAD.³³ It is therefore hardly surprising to find a higher diversion ratio, but it is not a ground upon which it can be concluded that a **[C]** owned store offers a significantly different competitive constraint to stores owned by the LADs upon Somerfield.
67. Indeed, when faced with positive evidence to the contrary, Mr Davies simply turns a blind eye to it. He dismisses at paragraph 63 the results in relation to high diversion ratios to Netto at 3 out of the 8 surveyed locations on the ground that the existing Netto store was extremely close. In fact, this is relevant as it is consistent with the analysis that, where a LAD is close to a Somerfield store in a particular location (as would be the case if a LAD were to purchase the stores that Somerfield proposes for divestment), the LAD is a significant competitive constraint.
68. Mr Davies’ refusal to have regard to the Netto data is also inconsistent with his analysis of the results for other fascias where he has not disregarded data because of their close distance. Thus Mr Davies relies upon the Co-op

³² More frequently occurring than multiple LADs in a particular location. Thus, for example, in Prestonpans, where customer diversion to **[C]** is 34.4%, there are 3 mid-range and 6 convenience **[C]** stores within the primary isochrone of the surveyed store.

³³ By way of illustration, among the 50 locations where the NOP survey showed diversion to a **[C]** store, the number of cases where the closest **[C]** was within 1 minute was 8 and within 5 minutes, 30. By contrast, among the 38 locations where the NOP survey showed diversion to a LAD, the equivalent figure for 1 minute was 5 and 5 minutes, 16.

average diversion ratio which is boosted by, for example, a 65% customer diversion ratio in Selkirk, where the Co-op store was also extremely close (0.2 minutes).

69. It is clear that the CC ought not to have had any regard to the NOP survey when determining the range of potential divestees. It was neither designed for nor suited to the purpose for which it is now prayed in aid.

(v) evidence from the Mintel report

70. The CC relies on a Mintel report at paragraph 6.43(d) of the Report showing that only 14% of adults used a LAD or Kwik Save at least once a week, whereas a majority of adults shop at one of the main chains at least once a week. The reason for this is, however, obvious – there are many more stores operated by the major chains than by the LADs and Kwik Save. It is therefore hardly surprising that many more people in total shop each week at the major chains. Furthermore, the impact of a competitor (shown in the hard evidence of the assessment at Appendix B) may not depend on frequency of shopping. The fact that the CC is driven to reliance on such obviously irrelevant matters demonstrates the weakness of their case on the limitation of range of potential divestees.

Conclusion on the second issue

71. Somerfield does not dispute that it is legitimate for the CC to take into account all relevant matters when determining the range of potential divestees. However, when the CC's reasoning is exposed to analysis, it is clear that of the five matters it took into account, only the competitive impact assessment is persuasive but it does not support the conclusions which the CC seeks to draw. As to the other four matters, neither individually nor collectively are they capable of supporting the CC's decision to exclude the LADs from the potential divestees.
72. The CC specifically found that the Stage 1 analysis alone was insufficient to address the competition issues arising from this acquisition. The competitor set was only used as part of an acknowledged conservative approach to Stage 1 where 48 potential problem stores were identified. It is the Stage 2 analysis, which of course included the impact of the LADs and other grocery retailers, that is determinative of the finding of SLC.

73. At [6.41], the CC expressly anticipates that other fascias “may also provide a more limited degree of competition, or effective competition in a limited number of areas, which we take into account in Stage 2 of our analysis”. At [6.43c], the CC acknowledges that its NOP Survey has demonstrated that there were areas where the LADs do seem effective competitors. The CC is inconsistent. It acknowledges that it must assess those local areas where LADs may provide effective competition in order for it legitimately to establish SLC, and yet when considering remedies, it excludes the possibility (against the evidence) that a LAD could enter a local market and provide effective competition to the remaining Somerfield/Kwik Save store(s).
74. For clarity, Somerfield observes that this aspect of the case does not simply concern the initial stipulated period. **[C]** Paragraph 49 of the Defence seriously downplays the importance of the point in stating that the LADs are only excluded for the initial stipulated period. That observation is in any event irrelevant to the issue whether the CC had the power to exclude them at all.

75. **[C]**

E. CONCLUSION

76. The restrictions on the stores which Somerfield is permitted to divest (issue 1) and on the identity of permitted purchasers for the initial stipulated period (issue 2) plainly affect Somerfield’s fundamental right to dispose of its property. Indeed, it may be noted that the CC has shown surprisingly little concern for the question whether Somerfield might get a fair price for divestment stores³⁴ and lack of concern for Somerfield’s right to retain the store of its choice (e.g. where more profitable) as set out above. This of itself is an indication that the CC has not adopted a proportionate approach to the interference with Somerfield’s legitimately acquired property.
77. Accordingly, Somerfield respectfully invites the Tribunal to grant it the relief sought at NoA [115]-[116] in respect of the matters raised in NoA [101]-[114].

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AIDAN ROBERTSON

21st November 2005

³⁴ See the Group’s comments at the Remedies Hearing: NoA/40/1008, lines 16-33.

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