Neutral citation [2003] CAT 23

IN THE COMPETITION APPEAL TRIBUNAL

Case: 1012/2/3/03

New Court
Carey Street
London WC2A 3BZ

16 October 2003

Before:

Sir Christopher Bellamy (President)
Mrs Sheila Hewitt
Professor Graham Zellick

sitting as a Tribunal in England and Wales

BETWEEN:

AQUAVITAE (UK) LIMITED

Applicant

-v-

THE DIRECTOR GENERAL OF WATER SERVICES

Respondent

supported by

NORTHUMBRIAN WATER LIMITED

Intervener

Mr Michael O'Reilly (instructed by Messrs McKinnells) acted for the applicant.

Mr Jon Turner and Miss Valentina Sloane (instructed by the Director General of Water Services) acted for the respondent.

JUDGMENT (Costs)

Introduction

1. On 5 August 2003 the Tribunal dismissed an appeal lodged on 20 February 2003 by Aquavitae (UK) Limited ("Aquavitae") regarding a decision made by the Director General of Water Services ("the Director") in respect of an allegation by Aquavitae that a number of water companies had abused their dominant positions contrary to the Chapter II prohibition imposed by the Competition Act 1998 ("the 1998 Act"): see [2003] CAT 17. The Tribunal's judgment determined as a preliminary issue that the decision challenged by Aquavitae did not constitute an appealable decision as to whether the Chapter II prohibition had been infringed within the meaning of section 46(3)(b) of the 1998 Act and that, consequently, the appeal was inadmissible.

2. On the occasion of the hearing of 5 August 2003 at which the Tribunal's judgment was handed down the Tribunal set a timetable for any written submissions the parties might be advised to make on the question of costs.

3. By letter of 13 August 2003 the Intervener, Northumbrian Water Limited, confirmed that it would not be making any submissions as to costs.

4. On 5 September 2003 the Registry received the Director's written application that Aquavitae should pay his costs of the appeal in full or, in the alternative, pay a proportion of his costs pursuant to rule 26(2) of the Competition Commission Appeal Tribunal Rules 2000, SI 2000 No 261 ("the Tribunal's Rules")[1]. Submissions from Aquavitae resisting the Director's application were received on 19 September 2003. In those submissions Aquavitae makes no cross-application for any of its costs of the proceedings, including the costs of this application by the Director. On 1 October 2003 the Director faxed certain further submissions to the Tribunal without formally seeking permission to do so. In the Tribunal's view these further submissions add little to the Director's previous submissions, but the Tribunal has nonetheless taken them into account.

[1] Aquavitae's appeal was originally lodged with the Competition Commission Appeal Tribunals established under the Competition Act 1998. By virtue of Articles 2 and 3 of The Enterprise Act 2002 (Commencement No. 2, Transitional and Transitory Provisions) Order 2002, S.I. 2003 no. 766, with effect from 1 April 2003 the appeal was deemed to have been made to the Competition Appeal Tribunal established under section 12 of the Enterprise Act 2002. On 20 June 2003 the Competition Appeal Tribunal Rules 2003, SI 1372 of 2003, came into force. Under rule 69 of those rules appeals not determined prior to that date continue to be governed by the Competition Commission Appeal Tribunal Rules 2000 S.I. 2000 no. 261 ("the Tribunal rules"). The costs provisions of both sets of rules are identical.

Summary of the parties' arguments

— The Director's submissions

5. The Director submits that he made every effort to avoid the commencement of the proceedings and that in correspondence, notably by a letter of 12 February 2003, the Director put Aquavitae on notice of the points that would be made against it in the proceedings and which have been upheld in the Tribunal's judgment. There was no need for Aquavitae to commence proceedings as the substantive question it sought to have resolved, namely what is the appropriate method of calculating the wholesale price of a supply of water, was one that would, in any event, have to be addressed by the Director in the course of the work needed to implement provisions of the Water Bill once enacted. Moreover, by letter of 3 March 2003 the Director warned Aquavitae that he considered its behaviour unreasonable. According to the Director, there is an important public interest in the Tribunal's costs jurisdiction being exercised so as to promote constructive engagement between parties in dispute and to discourage unnecessary litigation.

6. According to the Director, Aquavitae's conduct of the proceedings was "unreasonable and/or unnecessarily increased the burden on the Director's resources". In particular the Director draws attention to two specific matters. First, even if he had made an appealable decision, Aquavitae's failure to comply with the procedure required by section 47 of the 1998 Act would have rendered its appeal inadmissible in any event. Secondly, the notice of appeal was, according to the Director, unclear on key issues such as the source and content of the alleged decision and required the Director to request clarification by letter on three separate occasions. In addition the notice of appeal was accompanied by a significant amount of material of only peripheral relevance which nevertheless the Director and his advisers had to read and consider in detail.

7. The Director submits that even where a party has not behaved "unreasonably, frivolously or vexatiously" an order for costs may nevertheless be justified where an application is "unfounded": see *Hasbro UK Limited v Director General of Fair Trading* [2003] CAT 2, [2003] CompAR 59 ("*Hasbro: withdrawal*").

8. Finally the Director submits that the appeal was dismissed in its entirety and that the considerable work and diversion of Ofwat's limited resources from other ongoing investigations by the proceedings should be compensated by an order for costs against

Aquavitae. According to the Director his staff devoted 600 hours to dealing with the appeal, 400 of which were accounted for by Ofwat's in-house legal team, at a total in-house cost of some £12,936 with a further £26,185 having been incurred on Counsel's fees. If Ofwat is unable to recover those sums in whole or in part they must instead be borne by water customers as Ofwat's costs are recovered from licensed water companies, who, in turn, recover those costs from customers.

— *Aquavitae's submissions*

9. Aquavitae in its written submission of 18 September 2003 submits that in exercising its wide jurisdiction as to costs under rule 26(2), the Tribunal does not apply a general or rigid rule to the effect that losing appellants should normally be liable for a respondent's costs as well as their own, absent unreasonable conduct or other exceptional circumstances. In support of this proposition Aquavitae cites the Tribunal's judgments on costs in *Institute of Insurance Brokers v Director General of Fair Trading* [2002] CAT 2, at [54], explicitly accepted by the Office of Fair Trading (formerly the Director General of Fair Trading) in *Napp Pharmaceuticals v Director General of Fair Trading* [2002] CAT 3, at [18].

10. According to Aquavitae its conduct of the proceedings was not unreasonable. The Tribunal's judgment expressly indicated that there was force in the arguments put forward by Aquavitae: see paragraphs [189] and [202] of the judgment.

11. The Director's submission that Aquavitae failed to engage in the constructive attempts initiated by the Director to resolve matters without the need to resort to litigation is without foundation. In particular the points made in the Director's letter of 12 February 2003 were only being advanced 5 days before the deadline for appealing expired. There was no indication given that the Director was prepared to waive that deadline in order to attempt to avoid the need to bring the appeal. Aquavitae contends that it, not the Director, put forward the most constructive proposals to avoid the litigation, for example, by its suggestion that the matters in dispute should be submitted to a Queen's Counsel specialising in competition law for an opinion.

12. According to Aquavitae, the Director's argument that he is entitled to an order for costs because Aquavitae's appeal would have failed in any event, because of the failure to comply with the procedural requirements of section 47 of the 1998 Act, is

without foundation. The Tribunal expressly and deliberately declined to decide whether or not it would have found against Aquavitae on this point: see the judgment at [218].

13. As to the Director's submission that Aquavitae's application lacked clarity, Aquavitae points out that much of the appeal documentation was directed to the issue of retail competition in the supply of water, rather than to the question raised by the Director as to whether there was an appealable decision.

14. Finally, Aquavitae submits that, insofar as the Director's submissions on costs are based on the overall lack of merit of Aquavitae's case, they are ill-founded. During the course of the proceedings the Director, according to Aquavitae, made an important concession that there was nothing in principle preventing a person in Aquavitae's position from supplying water on a retail basis. Furthermore, having stated that he would consider Aquavitae's complaint on its merits, a statement that the Tribunal found gave rise to a legitimate expectation, the Director subsequently declined to do so. In those circumstances, the costs incurred in determining whether the appeal was admissible were in reality attributable to the Director's reluctance to answer the "real question" in the case, namely whether there had been an infringement of the Chapter II prohibition.

Analysis

15. Rule 26 of the Tribunal's Rules provides:

> "26. – (1) For the purposes of these rules "costs" means–
>
> (a) if the proceedings are taking place before a tribunal in England and Wales, costs and expenses recoverable in proceedings before the Supreme Court of England and Wales;
>
> (b) …
>
> (c) …
>
> (2) The tribunal may at its discretion, at any stage of the proceedings, make any order it thinks fit in relation to the payment of costs by one party to another in respect of the whole or part of the proceedings and, in determining how much the party is required to pay, the tribunal may take account of the conduct of all parties in relation to the proceedings.
>
> (3) Any party against whom an order for costs is made shall, if the tribunal so directs, pay to any other party a lump sum by way of costs, or such proportion of the costs as may be just. The tribunal

> may assess the sum to be paid pursuant to any order made under paragraph (2) above or may direct that it be assessed by the President or Chairman or dealt with by the detailed assessment of the costs by a costs officer of the Supreme Court …"

16. In *Napp Pharmaceutical Holdings Ltd v Director General of Fair Trading* [2002] CAT 3, [2002] Comp AR 160 ("*Napp: interest and costs*") the Tribunal at paragraph [22] made the following observations on rule 26(2):

> "[Rule 26(2)] gives the Tribunal a wide discretion on the question of costs, to be exercised in the particular circumstances of the case. There is no explicit rule before the Tribunal that costs follow the event, but nor is there any rule that costs are payable only when a party has behaved unreasonably. All will depend on the particular circumstances of the case."

17. The Tribunal has now emphasised on a number of occasions that the wide discretion conferred by rule 26(2) to award costs is designed to enable it to deal with cases justly. At this early stage of the development of the 1998 Act, the Tribunal is proceeding on a case by case basis, dealing with different, and not always foreseeable, circumstances as they arise. The Tribunal is also of the view that its decisions as to costs should not be allowed to harden into rigid rules: see generally *Institute of Insurance Brokers v Director General of Fair Trading* [2002] CAT 2, [2002] Comp AR 141 ("*GISC: costs*") at [39] and [48]; *Freeserve.com v Director General of Telecommunications* [2003] CAT 6, ("*Freeserve: Costs*") p.11, lines 13 to 24 and *Aberdeen Journals Limited v Office of Fair Trading* [2003] CAT 21 ("*Aberdeen Journals costs*") at [19].

18. In *GISC costs* the Tribunal made the following observations at paragraph 54 regarding the liability for costs of losing appellants under rule 26(2):

> "At present there seems to us to be force in the contention that a general or rigid rule to the effect that losing appellants should normally be liable for the Director's costs, as well as their own, could tend to deter appeals: see Lord Woolf in *AEI Rediffusion* at p. 1522D. That, it seems to us, could be seriously counter-productive from the point of view of achieving the objectives of the Act, particularly as regards smaller companies, representative bodies and consumers. Leaving aside frivolous or vexatious cases, or those liable to be struck out under Rule 8 of the Tribunal's Rules, that policy consideration should, it seems to us, militate against the Tribunal awarding the Director his costs against unsuccessful appellants, whether in proceedings under section 46 or 47, at least in the absence of unreasonable conduct or other exceptional cases."

19. We also note that in *GISC costs* at paragraph 52 the Tribunal expressly left open the question of whether cases involving regulated industries where the costs of statutory

regulation are recovered, in one way or another, from the industry itself may raise separate issues to those considered in *GISC* .

20. Bearing those considerations in mind we consider the application of rule 26(2) in the specific circumstances of the present case.

21. The Director's first argument in support of his application is that Aquavitae's appeal was unreasonably brought because the Director pointed out, before the appeal was lodged, in a letter of 12 February 2003, that the appeal was clearly inadmissible, and in any event unnecessary. In that letter the Director stated that as far as he was concerned he had not made any appealable decision that the Chapter II prohibition had not been infringed, and that the disputed issue that Aquavitae wished to have resolved, namely the calculation of a "wholesale" price for a supply of water, was one that would be resolved in the course of the work the Director would need to carry out in implementing the provisions of the Water Bill.

22. In our view Aquavitae did not act unreasonably in bringing its appeal, nor was it self evident that the appeal was inadmissible. In its judgment of 5 August 2003 the Tribunal indicated that, although ultimately unsuccessful, there was force in the arguments on admissibility presented by Aquavitae: see for example the judgment at paragraphs 189 and 202. At paragraph 196 of its judgment the Tribunal pointed out that, although Aquavitae's argument based on the Director's letter of 4 September 2002 failed, it did so "albeit by a narrow margin". At paragraphs 206 to 209 of the judgment the Tribunal also made plain that it was only the "exceptional circumstances" of this case, namely the introduction of primary legislation, which led the Tribunal to conclude that the case closure letter of 3 December 2003 was not an appealable decision.

23. Without repeating the detailed analysis to be found in the judgment, the situation in this case was that Aquavitae relied, in the alternative, on two letters from the Director of 4 September 2002 and 3 December 2002, respectively. The primary reason why, in the Tribunal's view, the letter of 4 September 2002 was not an appealable decision - despite the fact that it was circulated to all water companies - was that, in that letter, the Director undertook to consider any complaint by Aquavitae on its merits (paragraphs 187 to 191 of the judgment). Aquavitae then immediately made specific complaints against various water companies. Unfortunately, the Director did not, in the event, consider those complaints, as he had said he would in his letter of 4

September, but closed his file by letter of 3 December 2002. In the letter of 3 December 2002 the Director gave, as his principal reason for closing the file, the announcement in the Queen's speech on 13 November 2002 of the introduction of a mechanism for retail competition in the Water Bill. The Tribunal found that that was a genuine reason for closing the file which did not involve an appealable decision (judgment, paragraph 203).

24. However, the Tribunal also said that it could understand why, in those circumstances, Aquavitae may feel a sense of grievance "that the Director had not in fact considered its complaint on the merits" (judgment, paragraph 204). Even if Aquavitae did not in the end establish an "appealable decision", it does not seem to the Tribunal appropriate that Aquavitae should bear the costs incurred by the Director in establishing how it came about that he had not done what, in his letter of 4 September 2003, he promised to do, namely consider Aquavitae's complaint on the merits.

25. Moreover, in the Tribunal's view there was from the outset a degree of ambiguity about the meaning and status of the Director's letters of 4 September and 3 December 2002. Following an application by Aquavitae for further disclosure, the Tribunal invited the Director to make voluntary disclosure of documents relating to the question of whether he had made an appealable decision. That disclosure, which was supported by a witness statement by Mr Saunders, Ofwat's Director of Consumer Affairs, was material to the Tribunal's conclusions (see e.g. paragraphs 189 and 190, and 203) and considerably facilitated the Tribunal's understanding (judgment at 219). Self evidently, that disclosure would not have been made had the appeal not been brought. In all these circumstances in our view it was not unreasonable for Aquavitae to come to the Tribunal to have the status of the Director's letters investigated and the ambiguities resolved.

26. As regards the Director's argument that he made every effort to avoid the litigation, we acknowledge that there is an important and well-established public interest in prospective parties to litigation being encouraged to take reasonable steps to explore possible means of settlement in order to avoid the need to commence proceedings. However the Director's letter of 12 February 2003 did not indicate any willingness to investigate Aquavitae's complaint, but merely offered Aquavitae the possibility of participating in discussions about the implementation of the Water Bill. Moreover, that letter was received by Aquavitae only a short time before the deadline for appealing expired. The time for lodging the notice of appeal under rule 6(3) of the

Tribunal's Rules is subject to "strict limits … with very little or no possibility of extension …": see *Napp Pharmaceutical Holdings Ltd v Director General of Fair Trading* [2001] CAT 2, [2001] CompAR 21, at [28]. In those circumstances, we do not think Aquavitae acted unreasonably in proceeding to lodge its appeal despite the Director's letter of 12 February 2003. We note once again that the investigation of Aquavitae's complaint that was expressly promised in the letter of 4 September 2002 was not proceeded with by the Director, giving rise to an understandable sense of grievance on Aquavitae's part.

27. As to the Director's submission that Aquavitae's failure to comply with certain fomalities - since repealed - required by section 47 of the Act made it unreasonable to bring the appeal, the Tribunal expressly held that we were not deciding the section 47 point against Aquavitae: see paragraph 218 of the judgment. The observations at paragraphs 214 to 217 of the judgment about whether Aquavitae's letter to the Director of 9 December could be construed as an application to withdraw or vary a decision made pursuant to section 47(1), were made in the context of a finding that there was no appealable decision in respect of which an application under section 47 could have been made. We are not prepared to find, as the Director invites us to do, on some hypothetical basis that, if he had made an appealable decision we would inevitably have rejected Aquavitae's appeal on the basis of a failure to comply with the procedural formalities of section 47. In any event, in our view it would be wrong in principle to make further findings at this stage, in the context of an application for an order for costs.

28. As regards the alleged lack of clarity in the notice of appeal, Aquavitae provided clarification to the Director when so requested. We do not have the impression that the Director encountered any significant difficulties in preparing his defence. We note that the Director in his written submissions lodged for the case management conference on 21 March 2003 felt able to outline his case in some detail (see "Item 4", paragraphs 6 to 20). We also note that at "Item 5" of those submissions, the Director considered that it was not likely to be useful to request any further clarification from Aquavitae at that stage. At paragraph 22 of those submissions he stated, "the basis for deciding the issue of admissibility seems sufficient on the material now available."

29. Neither are we satisfied that the Director's submission based on the length of Aquavitae's notice of appeal, or the volume of annexed documents, justifies an order

for costs, even partially. Once the Tribunal directed that the question of the admissibility of the appeal should be tried as a preliminary issue the ambit of the case was significantly narrowed. The Director did not, in the event, have to plead this case on the merits. Many of the background documents, even if not directly relevant to the issue of admissibility, helped to place the case in context. Having had to work on the same bundle of documents as the parties, the Tribunal does not consider that the presentation of Aquavitae's notice of appeal and the documents concerned could of itself justify an order for costs against Aquavitae.

30. The Director submits, finally, that "the appeal was dismissed in its entirety and involved considerable expense and time on the part of the Director." Those expenses, if not recovered in whole or in part from Aquavitae, must be borne instead by water customers as Ofwat's costs are recovered from licensed water companies, who in turn recover those costs from customers.

31. As the Tribunal's previous judgments on costs set out at paragraphs [15] to [19] above explain, there is no general rule in appeals before the Tribunal under the 1998 Act that costs should be borne by the losing party. In the Tribunal's view, such a rule would run the serious risk of frustrating the objectives of the Act by deterring appeals by smaller companies, representative bodies and consumers, as the Tribunal made clear in *GISC costs* at paragraph 54. It seems to us that these policy considerations apply in cases such as the present. In particular it seems to us that potential new entrants to regulated sectors, such as Aquavitae, which do not appear to command substantial financial resources, are liable to be deterred from bringing appeals if the Tribunal were regularly to order that such appellants should normally be liable for the Director's costs, as well as their own, in the absence of unreasonable conduct or some other exceptional factor.

32. We understand the Director's concern that in the end the costs that he incurs in such appeals have to be borne in one way or another by the industry and, ultimately, its customers. However, looked at more generally, the system of regulation in the water industry, as in other regulated sectors, exists to protect a wide range of different interests, including those of the general public. In our view, the system as a whole will function more effectively if complaints can be brought and the regulator's decision can be challenged on appeal, if necessary. The costs incurred in a case such as the present are minuscule by comparison with the total revenues of the water industry taken as a whole, whereas the burden of costs falling on a small complainant,

acting reasonably, if unsuccessfully, is likely to be disproportionately heavy. We have already indicated that we consider this appeal was reasonably brought albeit not ultimately successful and in the particular circumstances of this case we consider that the Director's costs of the appeal should be regarded as part of the general costs of regulation in this sector.

Christopher Bellamy Sheila Hewitt Graham Zellick

Charles Dhanowa 16 October 2003
Registrar