**IN THE COMPETITION APPEAL TRIBUNAL**

Case No. 1104/6/8/08

Victoria House
Bloomsbury Place
London WC1A.2EB

Wednesday, 12th November 2008

Before:

THE HONOURABLE MR JUSTICE GERALD BARLING
(President)

PROFESSOR JOHN PICKERING
MR. GRAHAM MATHER

Sitting as a Tribunal in England and Wales

BETWEEN:

**TESCO PLC** — Applicant

and

**THE COMPETITION COMMISSION** — Respondent

and

**WAITROSE LIMITED**
**MARKS AND SPENCER PLC**
**ASDA STORES LIMITED**
**THE ASSOCIATION OF CONVENIENCE STORES** — Interveners

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# HEARING – DAY TWO

# APPEARANCES

Mr. Nicholas Green QC, Mr. Mark Hoskins and Mr. Julian Gregory (instructed by Freshfields Bruckhaus Deringer LLP) appeared on behalf of Tesco Plc.

Mr. Peter Roth QC, Mr. Daniel Beard, Ms Valentina Sloane and Mr. Ewan West (instructed by the Treasury Solicitor) appeared on behalf of the Competition Commission.

Mr. Tim Ward (instructed by Slaughter and May) appeared on behalf of Asda Stores Limited.

Ms Kassie Smith (instructed by Lovells LLP) appeared on behalf of Waitrose Limited.

Mr. Robert O'Donoghue (instructed by SJ Berwin LLP) appeared on behalf of Marks and Spencer Plc.

MR. GREEN: Yesterday before the break I was dealing with the question of best practice in relation to the conduct of an assessment of cost. Before I return to that, can I hand up a one-page note simply responding to the question that, Mr. Mather, you posed yesterday about para. 7.40 of the Competition Commission's report, and an observation made by Tesco. We checked the background documents which led to that sentence being included. It can be addressed very shortly. (Same handed) It is a very short point. The sentence in the report said,

> "Tesco, however, stated that it knew of no case where a planning application had failed solely because of the lack of identifiable need".

" The key in that sentence was the word 'solely'. The sentence reports one aspect of Tesco's submissions to the Commission about the planning regime is that Tesco had looked at those of its own applications which had been refused, and concluded that the refusal had not in any case been solely because of a failure to prove need. Other aspects of the planning test, such as the sequential test which the Commission refers to in its report, and the retail impact test, had also been failed.

We have set out an excerpt from the actual submission. The point is that it is not just the need requirement in the planning regime which constitutes a barrier to entry; it is also the existence of other requirements as so found by the Competition Commission. I hope that is helpful.

I would like to take you now to the Ofcom guidance on better policy making which is at Tab 22 of the authorities' bundle. This paper is concerned with the desirability of, and the method of, conducting impact assessments. There are a number of paragraphs that are of relevance particular to the analysis. I think it is appropriate to start with some of the context of this report so that you can see what Ofcom is seeking to achieve. Under s.1, para. 1.1 Ofcom makes what we submit is an elementary point of good regulation. At p.3 of the internal number of the report, the paragraph says,

> "The decisions which Ofcom makes can impose significant costs on our stakeholders and it is important for us to think very carefully before adding to the burden of regulation. One of our key regulatory principles is that we have a bias against intervention. This means that a high hurdle must be overcome before we regulate. If intervention is justified, we aim to choose the least intrusive means of achieving our objectives, recognising the potential for regulation to reduce competition. These guidelines explain how Impact Assessments will be used to help us apply these principles in a transparent and justifiable way".

They then cite from the Better Regulation taskforce of September 2003. They put in bold, because they plainly attach importance to the following quotation,

> "The option of not intervening . . . should always be seriously considered. Sometimes the fact that a market is working imperfectly is used to justify taking action. But, no market ever works perfectly, while the effects of . . . regulation and its unintended consequences may be worse than the effects of the imperfect market".

In s.5, which starts on p.12 of the internal numbering, Ofcom in a chapter entitled 'What stages are involved in an Impact Assessment?' explains the nature of the assessment. A preliminary observation that we make is that there is no magic, or no term of art, involved in the concept of an impact assessment. It is an integral part, we would submit, of proportionality and of reasonableness. It would be an integral part of any test of comprehensiveness or practicability. That would apply regardless of whether or not a statute specifically mandates a regulator to conduct an impact assessment. Indeed, a reflection of that is found in para. 5.1 of the Ofcom document which starts with this sentence.

> "A key principle is that an Impact Assessment should be proportionate to the likely impact of our decision".

Ofcom therefore links impact assessment with the concept of proportionality. We rely upon the Competition Commission's skeleton at para. 50. I will read it to you (because it is short and you need not turn it up),

> "The Commission fully accepts that it should take account of the relevant costs associated with its chosen remedies".

Then it refers to report paras. 11.381 et seq. That is p.23, para. 50 of the Competition Commission's skeleton.

So, the Competition Commission accepts that it must (a) take account of, (b) costs which (c) are relevant, and (d) which are associated with a particular remedy. We submit there is no sensible dispute between the parties that a proper assessment of the costs is required to be undertaken.

If one returns to the Ofcom document, Ofcom helpfully sets out the stages that it believes are involved in an impact assessment in para. 5.4. Again, we would submit that those six stages are inherent in any sensible assessment of costs, whether one puts it under the rubric of comprehensiveness, practicability or reasonableness. They are defining the issue we need to consider in identifying the citizen or consumer interests; defining the policy

objective; identifying the options; identifying the impact on different types of stakeholders; identifying any impacts on competition; assessing the impacts and choosing the best option.

That, we submit, is a very broad and reasonably accurate description of any impact assessment.

Ofcom also makes the point that the nature of an impact assessment will vary from case to case. They do not accept it is a single algebraic formula which you apply to any particular set of facts - it is applied flexibly and proportionately, depending upon the importance of the issue and a range of other factors. It is not therefore a precise term of art.

In the context of actually applying the test Ofcom starts with a proposition that we say is implicit in s.134 and which the Competition Commission accepts (because I showed you the paragraph in their guidance yesterday which reflects that) that the starting point is not to change anything.

Paragraph 5.13, p.14 of the internal numbering, says,

> "When identifying the possible options, we will generally start by considering the option of not changing the regulatory framework, either by not introducing regulation or by retaining existing regulation. This option - no new intervention - will be the benchmark or base case against which other options will be judged, i.e. what costs and benefits would be incurred additional to those which would be incurred if there were no new intervention".

In 5.25 Ofcom makes what we submit again is a very obvious point, that in choosing the best option for a remedy one needs to assess costs and benefits. 5.25, p.16, says as follows:

> "Choosing the best option will involve an assessment of the costs and benefits which would flow from the options selected. However, this will generally inform rather than determine our decision. There are two main reasons for this. First, fulfilling our statutory duties will often mean taking account of issues that would fall outside a narrow consideration of costs and benefits. Secondly, it will often be difficult to quantify all the costs and benefits, in which case, it may be hard to identify which option has the highest net benefit and choose an option solely on that basis. Nevertheless, every impact of the chosen option would result in costs and/or benefits. If such costs and benefits cannot be quantified (or it is not proportionate to quantify them) they should still be described and taken into account in making our decision."

We strongly endorse that paragraph. We submit that it is just common sense as much as anything. Again, we submit it would fall within each of the two questions which we posed as arising under s.134, the "whether or not" and "if so what remedy". We do not think there is anything unusual about the notion that you should take account of the costs and the benefits of what you are proposing to do. Nor do we suggest that there is anything unusual about a regulator, if unable to quantify a particular cost or benefit, taking account of it in a qualitative manner.

THE PRESIDENT: You say that they did not do either of those?

MR. GREEN: We say they did not do either of those. They have told us that they did not do either of them.

THE PRESIDENT: They have told you they did not do the first, did not quantify it, because it was too difficult.

MR. GREEN: There is no evidence that they took account of the costs. Perhaps at a later point ---

THE PRESIDENT: We are on benefits, are we not, now?

MR. GREEN: The benefits, yes. One simply reads the report and one sees what they did. The defence and skeleton tells us that they did not do it. There is no suggestion that as an alternative to quantifying it they carried out the following process of analysis. That is not in the defence or in the skeleton.

THE PRESIDENT: This has the statement that if they cannot quantify them they have to take them into account and that can only be done, you say, qualitatively, which must mean some kind of assessment, must it not?

MR. GREEN: Can I come back later to what we say the difference between quantitative and qualitative is, because we think logically one can work out a road map for any regulator to take in respect of any remedial decision. There is a logical process which should be identifiable which would inform the steps which a decision maker should take.

Paragraph 5.30 under the heading "Analysing costs and benefits":

> "A key part of our assessment of which is the best option will be an analysis of the benefits and costs that would flow from each option. In doing so, we expect to apply the following principles:
>
> - All significant impacts of regulation should be included (regardless of whether the resulting costs and benefits can be quantified) and the types of costs and benefits should be spelled out e.g. whether the costs or benefits are financial or non-financial.

- In analysing costs and benefits it is necessary to apply the principle of proportionality, which means it will often be appropriate to focus on the most significant costs and benefits and not spend a disproportionate amount of time considering costs and benefits which are relatively minor.
- As far as possible, it should be made clear who bears the costs and who receives the benefits, including those flowing from the impacts on the interests of particular groups or sub-groups of stakeholders. Assumptions should be clearly spelt out.
- Only costs and benefits that would be reasonably incurred as a result of an option being implemented (as opposed to costs and benefits that would be incurred anyway) should be taken into account.
- Where there is significant uncertainty about the impact of an option, it is good practice to present an analysis of the sensitivity of the results to changes in some of the most important variables. This should help ensure that the Impact Assessment and the final policy decision are more robust.
- The cost of complying with regulation e.g. of providing regulatory information or adopting new technical requirements, should be identified if possible, as well as the possible negative impacts of regulation.
- Dynamic benefits and costs should be taken into account e.g. regulation may have a wider benefit in terms of enhancing the productivity and competitiveness of the sector.

**Quantifying costs and benefits**

- Costs and benefits should be quantified where possible, although benefits in particular may be hard to quantify as they tend to be more uncertain and are often spread across many citizens or consumers.
- Precise quantification will often not be possible and we should avoid spurious accuracy. Where quantification is possible, it will often be partial i.e. it is not possible to quantify all the relevant costs and benefits.
- Where costs and benefits cannot be quantified precisely, we should aim to give broad estimates e.g. in the order of £x million, or ranges of costs and benefits e.g. between £x million and £y million. It is also helpful to form an idea of the relative size of the respective costs and benefits. As a minimum, costs and benefits should be described qualitatively.

- Where it is possible to quantify costs and benefits, we will use the discount rate recommended by HM Treasury (unless there are specific reasons to do otherwise) to discount future costs and benefits and work out the net present value."

Then there is a section, 5.31 onwards, in which Ofcom states:

"It is also important to consider the risks relating to particular options, for example, the risk that the intended impact would not be achieved or would be delayed by problems with implementation. An option which has a high net benefit, but which carries a high risk, might be less attractive than a lower risk option which has a lower net benefit. The degree of risk will be influenced by the likelihood of it occurring and the extent to which it may be possible to mitigate the risk."

Then there is a section on unintended consequences.

We submit that the approach adopted by Ofcom makes good sense whatever the statute says, whether it uses the words "impact assessment", "costs benefit analysis", "practicability", "reasonableness" or "comprehensiveness", it is all very much of a one.

A further reflection of the importance of that approach is found in the Green Book which is at bundle 4, tab 76. With regard to this document, the Competition Commission expressly claims in its defence that the approach that it adopted to quantification was consistent with this document. The reference to that is Competition Commission defence, para.105, which is file 5, tab 1, p.3490. Paragraph 105 of the defence says as follows:

"Far from falling …"

then they quote the Tesco allegation –

"… '*far short of satisfying Treasury guidance on how policy proposals should be reviewed'* as alleged by Tesco, the Commission's approach to quantification is consistent with the Green Book guidance, which cautions against being '*spuriously accurate'* and requires quantification of costs and benefits only where this is '*possible and meaningful'*; see the extracts cited by Tesco …"

So the Competition Commission's position is that their approach is consistent with the Green Book, but the only point that they rely upon is that the Green Book does not require them to engage in impossible and unmeaningful quantification, and we are not suggesting that if quantification is impossible that they should do so. We submit the Green Book says, as does the Ofcom guidance, if quantification is not possible there are numerous other techniques which should be taken account of and which were not taken account of in the present case. So they purport to be acting in compliance with the Green Book, and the

Green Book is an HM Treasury document, it has a general application. It identifies a process that all government departments and/or decision makers should adopt in relation to decisions which have an impact on – to use the jargon – "stakeholders". Paragraph 2.3 on p.3193 of the bundle, defines the relevance of assessment of costs under the heading: "The Role of Appraisal". It says:

> "Appraisals should provide an assessment of whether a proposal is worthwhile, and clearly communicate conclusions and recommendations. The essential technique is option appraisal, whereby government intervention is validated, objectives are set, and options are created and reviewed, by analysing their costs and benefits. Within this framework, cost-benefit analysis is recommended, as contrasted with cost-effectiveness analysis below, with supplementary techniques to be used for weighing up those costs and benefits that remain unvalued."

Then they define "cost-benefit analysis" as:

> "Analysis which quantifies in monetary terms as many of the costs and benefits of a proposal as feasible, including items for which the market does not provide a satisfactory measure of economic value."

They say "cost-effectiveness analysis is:

> "Analysis that compares the costs of alternative ways of producing the same or similar outputs"

But it does not involve any analysis of the dis-benefits. There is therefore a slight difference between the two approaches.

3.2 and 3.3 the Treasury says that cost analysis is relevant in cases of market failure – p.3201 of the bundle under heading: "Reasons for Government Intervention".

> "3.2 This underlying rationale is usually founded either in market failure or where there are clear government distributional objectives that need to be met. Market failure refers to where the market has not and cannot of itself be expected to deliver an efficient outcome; the intervention that is contemplated will seek to redress this. Distributional objectives are self-explanatory and are based on equity considerations."

So a reason for intervention which justifies the approach proposed is a market failure which would precisely describe the exercise in broad terms which the Competition Commission was engaged in.

> "3.3 Government intervention can incur costs and create economic distortions. These must .."

So the Treasury believes this is a mandatory part of the exercise, it is that important –

> "… be taken into account to determine whether intervention is warranted. For example, a regulation may be successful in addressing a particular market failure, but might also involve other costs that mean overall it is not worthwhile."

So the binary choice of "whether or not" is reflected and acknowledged to be important at the highest level.

At 5.24 and 5.25 at p.3211 of the bundle, here the Treasury say that one should examine all the benefits and one examines the costs, there are no benefits if costs exceed benefits and it says that one gives estimates if precise quantification not possible.

> "5.24 The purpose of valuing benefits is to consider whether an option's benefits are worth its costs, and to allow alternative options to be systematically compared in terms of their net benefits or net costs."

I pause there, a netting process, a balancing process is one contemplated by the Treasury as integral.

> "The general rule is that benefits should be valued unless it is clearly not practicable to do so. Even if it is not feasible or practicable to value all the benefits of a proposal it is important to consider valuing the differences between options.
>
> 5.25 In principle, appraisals should take account of all benefits to the UK. This means that as well as taking into account the direct effects of interventions, the wider effects on other areas of the economy should also be considered. These effects should be analysed carefully as there may be associated indirect costs, such as environmental costs, which would also need to be included in an appraisal. In all cases, these wider effects should be clearly described and considered."

A point I think one is bound to make there is that the point that comes out of that is the importance of the net approach. Clearly statute may circumscribe the exercise slightly because the Competition Commission might say: "It is not for us to take account in a recommendation of environmental consequences, that is for somebody else to take account of in deciding whether to accept our recommendation." So there may be modifications but the underlying point is the one that we rely upon.

Finally:

> "5.29 Where it is concluded that research project to determine valuations is not appropriate, a central estimate together with a maximum and minimum plausible

valuation, should be included. These figures should be included in sensitivity analyses to give assurances that benefit valuation is not critical to the decision to be made. A plausible estimate of the value of a benefit or cost can often be drawn out by considering a range of issues which hare summarised in Annex 2."

The word I think we would alight on in para. 5.29 is the word "plausible". Assessment is not an exercise in perfection, it is an exercise in the art of the possible. One is trying to do the best that one can in order to arrive at a result which will inform a decision; necessarily it will have a varying degree of robustness, but that does not mean to say that it should not be done simply because the result may be more or less reliable in any given case.

PROFESSOR PICKERING: I feel you are about to move on – is that correct?

MR. GREEN: Sort of but not quite – do ask your question anyway.

PROFESSOR PICKERING: Thank you. I did not want to interrupt at an inconvenient point. Could I just ask you, in relation to competition authorities, they have a legislative requirement to conduct certain investigations and go about things in a particular way. The documents to which you have drawn our attention, both the Ofcom and the Green Book document do not distinguish between what one might call "macro-assessments" and "micro-assessments" of individual policies and recommendations. I just wonder, offering you both those issues whether in fact you would see that there could be circumstances in which the generality of the Treasury and the Ofcom approaches might be considered to be not applicable to the work of, say, the Competition Commission because they are acting under legislation. Furthermore, whether to require this further impact assessment in even more detailed form – but you are obviously saying should go beyond the normal way in which recommendations for amendments to policy are advanced by such a body, whether these are in fact proportionate in themselves recognising that significant costs of money and time are already incurred and that probably the implications are that to do this as well would further add to the cost burden. Do you see the point I am inviting you to help me on, Mr. Green?

MR. GREEN: There are a number of answers to that. First, we are concerned here with a market investigation. There is plainly micro-analysis involved, but it is a macro-exercise; one is dealing with the operation of an entire market segment. The Green book in paras. 3.2 and 3.3 specifically refers to market failure and remedies adopted to address market failure as an instance where this approach should be adopted. The Competition Commission, in its defence, at para. 50, says that it was purporting to act consistently with the Green Book and there is nothing in the Ofcom document, or in this document, which cannot be applied

directly to the exercise required under s.134. They are very basic requirements. One is simply saying in the main, "You must measure both the costs and the benefits. When you do that we accept that it cannot be performed in all cases with 100 percent accuracy, but that does not mean to say that you do not perform an exercise. There are sub-optimal exercises that you perform which involve assessing ranges, scenarios, sensitivity analyses, and if you cannot do that, you then resort to descriptive, qualitative analysis". All of that is very broad brush and it is exactly what the Competition Commission say they were purporting to do. So, there is nothing in this which suggests it cannot be transposed and should not be transposed to the competition field. The Ofcom document, of course, is applying across micro, as well as macro, issues. So, they do not differentiate in their guidance.

MR. MATHER: If I could follow that interesting line of discussion a little further, the Green Book was originally designed for infrastructure projects, and has developed in the way you describe. The Ofcom work is an example of a sector regulator in operation across government. The National Audit Office has reviewed, from time to time, the way impact assessments work. Often its reports have been very critical. It has said that departments have not done them; there are not enough numbers in them; they are not adequate. Can you help us by saying when that inadequacy to which those NAO reports bear testimony should prove fatal to a policy decision, and when it is something where departments should be encouraged to do better next time?

MR. GREEN: I think there are two points. First of all, the Green Book itself contemplates - as does the Ofcom document - a proportionate approach to impact assessment. So, one takes account of the nature of the exercise to be carried out by reference to the exercise that you are undertaking. So, the Green Book is intended to cover a range of different circumstances - not just large capital projects, procurement exercises. It covers market failure exercises. Secondly, when will a failure prove fatal? Well, when we are dealing with the Competition Commission, which is subject to a statutory regime, you have a statutory framework to apply. The starting point is to ask what questions the Competition Commission must ask itself. In a judicial review, one simply goes on then to ask, "Are there relevant considerations which the Competition Commission has not asked itself?" If the answer to that is, 'Yes, there is no real suggestion these would not be material errors', that sounds in judicial review. So, one has an analytical framework for a judicial review which takes one to an answer. One simply works one's way through the questions in 134 and 138, and you ask yourself, "Have they addressed the relevant question?" Everybody

accepts, including the Commission, that they must assess the costs. They fully accept that. We say they have not done so. We say they are required to assess the benefits of a test against the AEC. Well, they do not say they should not do so - they say they could not do so. Frankly, if they accept they have to analyse the costs of the competition test, then it would be ludicrous for them to say they should not also, in principle, assess the benefits. They are really two sides of the same coin. There is no difference in principle between the two of them. So, there should not be a difference in principle between us. They simply give a shrug of the shoulders, and say, "It's all too difficult". We say two things (which I am going to come on to), "(a) If that is so, it rebounds in law on the s.134 analysis; but (b) in any event, it is utter nonsense to say they could not carry out this exercise because they did, in relation to the AEC, and they have a veritable mountain of information which actually bears upon the very things they say they did not assess". We can prove to you that they did actually assess those very points. I am going to deal with that.

Unless I can assist further with this point -- The other three paragraphs I wanted to just pick up in the Green Book (and I will do this quite quickly) are at 5.69 -- When one is assessing uncertainty, which is always recognised to be a problem for regulators, one should undertake sensitivity analysis. The Treasury says that,

> "Sensitivity analysis is fundamental to appraisal. It is used to test the vulnerability of options to unavoidable future uncertainties. Spurious accuracy should be avoided, and it is essential to consider how conclusions may alter, given the likely range of values that key variables may take. Therefore, the need for sensitivity analysis should always be considered and in practice dispensed only in exceptional cases".

So, that is one approach to the sub-optimal - in other words, if you cannot quantify something precisely you engage in a sensitivity analysis. Another (and if I can use the term) sub-optimal approach is scenarios, which are referred to in para. 5.72.

> "Scenarios are also useful in considering how options may be affected by future uncertainties. Scenarios should be chosen to draw attention to the major technical, economic, and political uncertainties upon which the success of a proposal depends. Considering scenarios needs to be proportionate. It may take the form of asking simple, 'What if--?' questions for small and medium-size projects, but extend to creating detailed models of future states of the world for major policies and large programmes. The expected NPV (net present value) can be calculated

for each scenario. It may also be helpful to undertake some sensitivity analysis within a scenario".

They also deal with un-valued costs and benefits in para. 5.76 and following. But, I will just pick up 5.76 and 5.78.

"Costs and benefits that have not been valued should also be appraised. They should not be ignored simply because they cannot easily be valued. All costs and benefits must therefore be clearly described in an appraisal and should be quantified where there is possible and meaningful.

5.78 The most common technique used to compare both unvalued costs and benefits is weighting and scoring (sometimes called multi-criteria analysis). The basic approach to weighting and scoring involves assigning weights to criteria, and then scoring options in terms of how well they perform against those weighted criteria. The weighted scores are then 'summed' and these sums can be used to rank options. An even simpler method is to list the required performance criteria (sometimes called critical success factors) and assess options in terms of whether they meet them or not.

The only point that one draws from that I think again is a common-sense point, that even if one has an unvaluable cost and an unvaluable benefit, one can still get a handle on the scale and magnitude of the cost or the benefit".

Now, in relation to the conclusions that we draw from this exercise there are a number of points I would like to make. The first is that we accept there is no requirement to achieve spurious accuracy. That is plainly common ground between us. By the very nature of the adjective 'spurious', it indicates the answer. If it is false, then it is plainly something which should be avoided.

The second point is that we submit that the required analysis is an exercise in the art of the possible. We submit that in logical common-sense terms it is possible to identify a series of stages that the decision-maker should go through. This matrix should be applicable towards any decision that the Competition Commission makes. It can be taken in a small number of stages. First, the Commission should identify the links in the chain of cause and effect between the proposed remedy and the AEC - in other words, in logical terms, how will the competition test eliminate or address the AEC? This is a description process. You are simply setting out the links in the chain of causation. Put another way, if the Competition Commission is unable to identify the steps in the chain of causation, then manifestly there can be no justification for imposing any remedy because you would not be

satisfied that the remedy would have any impact upon the AEC. So, Stage 1 is merely a descriptive listing of the steps in the chain of causation.

The second stage is for each of those identified steps to examine the extent to which they can be quantified. It follows that quantification is not a perfectly balanced equation, it is the exercise of the possible, so one would use ranges, sensitivity analyses, scenarios, etc, and your aim and your object is to arrive at the most accurate estimate that you are able to arrive at. I emphasise the word "estimate", because it accurately reflects both what the Competition Commission said it did in relation to the AEC, but also because it imports the notion of a degree of uncertainty.

The third stage is to apply qualitative assessment where the quantitative is not feasible, or because there may be many different situations arising where the quantitative analysis is partial, you may combine the qualitative and the quantitative assessment in order to improve the accuracy of the estimate. This qualitative assessment will involve many of those steps which Ofcom itself identifies and entails setting out the assumptions that you are employing to assess the cost or the benefit and describing how strongly the assumption can be posited or how weakly it can be posited, what the risks are, and describing how large the risks are in descriptive terms, qualitative terms. If you have the steps in the chain of causation it is a straightforward task to describe and assess how strong or weak each of those steps in the chain of causation is.

Fourthly, and finally, you draw your conclusions from the combined qualitative and quantitative assessment, and you will identify the ranges and you will identify how strongly or weakly your conclusion is able to be posited. Indeed, one can see that the Competition Commission itself applied precisely this process in determining the scale of the AEC. One can demonstrate that quite easily in the Report itself at para.10.14, which is p.179 of tab 1 of file 2. You might want to put as a side note to 10.13 "see also paras.22 to 24, p.12", because it is evident from a combination of these two sections that the Competition Commission in identifying an AEC which it considered sufficiently certain of to justify a remedy – in other words, it got to this level of confidence and it was able to rely upon that confidence to trigger a legal remedy – it relied upon a wide range of assessments, ranges, scenarios, and sensitivity analyses. For example, in relation to the number of larger grocery stores that were highly concentrated, it gave a range of 11 to 27 per cent (that is para.22). In paras.10.13 and 10.14 the Competition Commission makes the point:

> "It is difficult to estimate directly the scale of consumer detriment …"

So their starting point is that the measurement of the AEC is, itself, difficult even to estimate, not measure precisely, the process of estimation is difficult. They say in the second sentence of 10.14:

> "We are, however, able to estimate, to some degree, the additional profits that grocery retailers earn as a result of weak competition. We estimate that the effect of weak local competition on store-level profit margins allows large grocery retailers to earn an additional £105-£125 million in profits a year …"

So we get a range with an almost 20 per cent difference of profitability, or excess profitability, and they calculate this is around 3 per cent of annual profits.

Again in 10.15 they say:

> "Weaknesses in local competition also result in higher national prices than would otherwise be the case. The scale of the impact on national price levels arising from weak local competition, while difficult to measure, is potentially very substantial."

So in relation to this they rely upon a hypothesis based upon something which they concede is difficult to measure. So they talk about the potentiality of an impact being substantial. So they are prepared to draw a conclusion in very broad terms about an impact – in other words, it is substantial – even though it is difficult to measure.

Equally, in 10.16 in relation to the supply chain:

> "… it is difficult to place a value on the cost of lost investment and innovation that would happen in the future."

They are able to attribute a value "is of the order of £70 billion", and they then say that they derive from that that the scale of the supply industry is such that "even a small loss is likely to have significant detrimental impact".

Then 10.17, given these considerations they are sufficient to justify remedial action.

So the inability to operate a precise exercise in the eyes and minds of the Commission was sufficient to trigger a legal consequence – in other words, the imposition of a remedy under s.134. No spurious accuracy, they did the best they could, they engaged in ranges, speculation based upon the existing information. The finding of AEC was an exercise in the art of the possible and the Competition Commission saw no difficulty with that exercise.

In response to that the Competition Commission now says when you measure the benefits of the competition test that it is an impossible task, albeit one contrasts their position in para.102 of the defence with para.50 of the skeleton, that they accept that they have to take

account of the relevant costs associated with the remedy. So there is no dispute in principle that they should take account of the costs. They simply say it is too difficult.

THE PRESIDENT: Do you say that that was good enough? I think you accept, do you not, because you do not challenge it – I know this is not the point you are on – in relation to AEC you say that that was as much as they could do, or at least you are not going to challenge it?

MR. GREEN: What we can say we have done is that we have examined the process that the Competition Commission adopted to come to its decision. This is the tip of the iceberg, this is simply their conclusions. There is a veritable Himalayan mountain of data underneath it which they found difficult to draw estimates and conclusions from. We are not able to say in the context of a judicial review that they failed to address their mind to relevant facts and considerations because they performed the exercise, as we put it, of the possible, and they came to conclusions and we have not challenged it. Whether we agree with it is an entirely irrelevant consideration, because this is a judicial review and we are concerned with the process that they were engaged in, whether they addressed their mind to relevant considerations.

THE PRESIDENT: You make a point about the degree of uncertainty, do you not?

MR. GREEN: Yes.

THE PRESIDENT: You have not got on to that yet.

MR. GREEN: What I am doing at this point is showing that when they measured the AEC they did not adopt the approach which they espouse in para. 102 of their defence. They accepted that simply because you could not quantify a detriment it should not mean to say you should not assess it, and they did the best they could on the basis of the evidence that they had. That is the approach which we say they should have adopted in relation to the benefits and, indeed, costs. That is the point now I am coming on to which is the implications of the position they have adopted. I am going to show you in just a couple of minutes precisely what they did do because in respect of everything they say there is this high degree of speculative-ness or uncertainty we can prove by reference to the findings in the report that they actually carried out each and every one of those steps themselves already. They had done the work. Everything they cite as an uncertainty or an impossibility in para. 102 they have done and they have drawn conclusions from each of those alleged uncertainties.

But I want to ask and pose a hypothetical question: what if they are right? What if it is an entirely impossible process to carry out? In those circumstances we submit that if the

Competition Commission is correct, and you find that they are correct, that the exercise is an impossible one to perform, then we submit that s.134 cannot be answered in favour of a grant of a remedy. If one stands back from the process in s.134 and put that conclusion under the heading of "comprehensiveness, practicability and reasonableness and proportionality", if one is not able to say that a remedy will exert any particular effect because it is impossible to quantify, how can one say that the package of remedies that one adopts is comprehensive; you simply do not know whether the remedy is comprehensive as a solution – which is what comprehensiveness relates to – a solution to the AEC. Therefore in the context of comprehensiveness, which is a factor they must take into consideration they must come to the conclusion that they do not know whether the remedy is comprehensive because if you have no idea how it relates to the AEC you cannot possibly come to form a view on it. If you cannot form a view on it we submit that in law that would weigh very heavily against the grant of any remedy. We do not submit it is decisive because it is not decisive in the Act, it is simply a factor which the Competition Commission must take into account, but it would weigh very heavily against the grant of any remedy.

MR. MATHER: Can I take you back to something you said a moment ago? You said everything they cite as uncertain and infeasible they have done – I think I have captured what you said. Could you expand on that a little? Does that mean that the necessary quantification or qualitative assessment has been done but has not been made explicit?

MR. GREEN: It has been done for another purpose. If I can answer the question very, very literally, you asked can I do it shortly? The answer is "no", but I will do it in about five minutes, if I may and then I will do it quite comprehensively, because that is the issue I am going to come on to once one poses this legal hypothetical question "what if?" If they are right that it is an impossible task we submit that there is only one answer in law that one can come to when one applies the s.134 test, and you simply ask yourself under the three principle considerations that the Competition Commission is required to address: comprehensiveness, practicability and reasonableness, what answer you lead to. "Comprehensiveness" I have just addressed. "Practicability" the same answer must apply. If you cannot assess the remedy because you have no idea when it will occur, where it will occur, who will come into the market and cure the market and so on and so forth, if you cannot assess that how do you know whether it is practicable, and if you do not know whether it is practicable how can you answer the question that it is something which would lead you to adopt that solution, that remedy? If you do not know you should not adopt any

remedy at all, the bias should be against action, and particularly not that action, if you simply have no idea because it is just not feasible, not possible, and too speculative. Why is it practicable to impose that?

THE PRESIDENT: Supposing you take the view that it will come right over time? You cannot give a complete handle on it but you have formed the view from everything you have looked at that along with the package this will provide some contribution to things coming right over time?

MR. GREEN: If there was a mechanistic answer, as I said in relation to ground one, if they are right that barriers to entry are so low that the remedy will resolve itself, I think I would concede that the question of timing would largely be irrelevant. If the barriers to entry are low one is entitled to assume that the market will self-rectify within a reasonable period of time and, even if you cannot quantify it, because the barriers are low then one should not worry about anything else and indeed that is the position the Commission took in relation to the mid ----

THE PRESIDENT: Mixed stores, or small stores.

MR. GREEN: That is right.

THE PRESIDENT: They thought there was not a market problem.

MR. GREEN: Because there were no barriers to entry, but in relation to the large grocery stores they said there was a barrier to entry. If there is a barrier to entry then timing becomes a critical issue because prima facie the speed at which the remedy will bite is going to be measured in the long term, and that is the corollary of there being barriers to entry; it is the opposite of the Competition Commission's finding for the mid-range market. If that is the case, then plainly unless the Competition Commission is saying in their submissions that they accept that when they use the word over time that means in the very long term, which I am sure that is not what they are saying, they are saying it will occur within a reasonable period of time – if that is their answer then that is just pure madness, because let us assume it takes 10 years how can it possibly be said that is a remedy which is comprehensive or reasonable and practicable, but that is not what they mean. They are purporting to convey the impression that things will happen within a reasonably short period of time, not a very long period of time.

THE PRESIDENT: How do you know that though? We do not know that, they have not put a handle on it.

MR. GREEN: There is no handle on time at all. The only handle we have, I think I am right, it is para.52 of the skeleton, where they say there is no reason to believe it will not be the

same time as under the previous present arrangements – it is hard to know what they mean by that. It is not analysed in the report, it is not something which fairly and squarely they have addressed their minds to. When they have addressed it, it is in the other context of demonstrating that entry is very difficult, it either does not occur or, if it does occur, it takes a very long period of time which demonstrates the existence of barriers to entry. So they addressed it but for a different purpose. They have not addressed it in this context.

The only other legal point that arises is in relation to the concept of "reasonableness" which we submit incorporates proportionality. We do know that the Competition Commission concluded that the remedy imposes a major burden on incumbents. They did record at the very least that 24 per cent of all grocers will be stymied by this. There are other statistics in the report which demonstrates that a very large number of the high concentration areas are in fact monopoly areas. Appendix 6.1 indicates that over 60 per cent of all the areas they found as concentrated will be monopoly areas, which means that there is no other incumbent who could expand, so they are the person who would naturally expand. 24 per cent of all grocery stores will be subjected to the limit. So there is a burden imposed, it is the cap on growth and the only point here in terms of reasonableness is this: they recognise they are imposing a burden. Proportionality means that the burden has got to be proportionate to the benefit; you are simply balancing the burden on the company – those subject to it against the objective you are seeking to achieve. If you have not measured either the cost or the benefit, how can you answer the question about proportionality. You have not addressed your mind to the considerations which will enable you to come to a legal answer.

So in relation to the three considerations that they are required to address their mind to under s.134 in law we say that if you cannot make the assessment you cannot answer the questions; and we submit a further consequence in law, if you cannot answer the questions you cannot justify a remedy; you err on the side of not imposing that remedy, it is disproportionate and unreasonable to do otherwise.

THE PRESIDENT: So that is the submission you make, that if they are right in what they say in para. 102 ----

MR. GREEN: Precisely, yes.

PROFESSOR PICKERING: Mr. Green, why do you say that in the monopoly areas there could be no other entrant?

MR. GREEN: I do not say 'no other entrant'. I say that in a monopoly area, if there is no entry then you do not have another incumbent who could expand.

PROFESSOR PICKERING: No. I am sorry. I may have got the wrong nuance, but I thought you were implying that that was unlikely.

MR. GREEN: No. I am suggesting actually that according to the Competition Commission's own findings in Appendix 6.1 - I do not think it is an appendix I have taken you to so far - they actually do an analysis of the number of areas which are monopoly areas and highly concentrated. It is a very high percentage. I simply draw from that the conclusion that the remedy in the competition test is to prevent incumbents from expanding, and if you have a high incidence of monopoly areas, then obviously there is nobody else who can take up this slack by extension - it has to be through new entry.

PROFESSOR PICKERING: But would you think that it may be that if the competition test were to come into force, that that might itself lower whatever barriers to entry there are in those monopoly areas, and therefore provide somewhat more of an incentive to somebody else to come in?

MR. GREEN: This is the U-bend point that I referred to yesterday - you squash one. What impact will it have on new entrants? Again, the Competition Commission's own findings indicate that when you have persistent monopolies there is no new entry even if there are no extensions - that is even in areas where there is room for an additional store. So, the evidence which the Competition Commission itself found and relied upon to establish the barriers to entry indicate very strongly that the whole question of extensions is irrelevant in large part to the question of new entry.

PROFESSOR PICKERING: I am not talking about extensions. I am talking about new entry. All analysis is obviously subject to *cateris paribus* conditions. Surely, the implication of what we are talking about in this case is the proposal that there be a competition test which would actually remove those existing conditions. So, I do not think that one can argue in that particular case from the present situation forward, because if the remedy is likely to be effective then circumstances will change.

MR. GREEN: Yes. But, with great respect, the obstacle to new entry is the planning regime. This does nothing to the obstacles found by the Commission to exist flowing out of the planning regime. The costs of applications, the uncertainty, the unavailability of land, the time it takes to compile land, and so on, and so forth -- Those are independent, free-standing obstacles which arise quite independently of the mere fact that you have an incumbent sitting there, squatting in the market. The barriers to entry which they found to exist are quite independent of that, and those persist into the future. So, if you simply take out one aspect of the equation - namely, the ability of the incumbent to expand, and you do

nothing in relation to the other things, then the question is: How are new entrants going to find it easier simply because you are putting a ball and chain on the incumbent? The answer is: If you look at their findings, there is nothing to suggest that there is a causal connection between addressing that one aspect of the market and new entry. There is no explanation as to why simply squashing the incumbent will have a material impact in any way upon new entry when you have not changed the need requirement; the sequential requirement for planning; when you have not done anything which will make land more available; when you have not speeded up the planning process, and so on, and so forth. When all of those remain, and will remain in the future, the Competition Commission has not answered the question as to why new entrants will find it easier. That is why the persistence analysis is important - because it demonstrates that even where you have unmet demand but no extension - and so one has got a proxy for suppressing the incumbent who is not allowed to and does not extend -- you have still got a very high level of persistence and no new entry over a very long period of time. So, it is a good laboratory experiment. That is why I say that all the evidence simply points in one direction. If the Competition Commission is right with its theory, one would expect to see a chapter, or twenty paragraphs, explaining it. There are none.

PROFESSOR PICKERING: My final observation on this particular point: if the competition test is brought in, just looking at businesses facing an incumbent in a particular local market - it does not have to be your clients; it may be one of the others - does the competition test and therefore the knowledge if passed that this precludes the incumbent expanding -- does this not, as it were, take away what one might call reputational barrier and actually take away some of the risks which perhaps make the accumulation of a land bank, etc. very unattractive because the fear is that the incumbent will get the permission? The implications of a competition test surely are to change the whole environment in which business decision-making would take place?

MR. GREEN: Again, there is no explanation of how, or why, any new entrant should consider that it is worth its while to enter a market simply because it knows that Grocer X is curbed. There is no evidence of that. There is no analysis of that. If that were a factor, one would have expected to see indications of it in the persistence analysis - in particular where there is very substantial unmet demand. Why has a new entrant not come in? Is it because it is thought that the incumbent will simply expand? The answer is that there are numerous areas where there is plenty of room for a new store. So, not just an extension. It is not a case where an extension could block a new store. This is a new store. There is no reason to

suppose in those circumstances that a planning authority would favour an incumbent over a new entrant - in fact, absolutely no reason to suggest that. The persistence analysis makes that point very strongly. Many areas they found where there is sufficient demand for a new store, where there is no new entry. That is because the barriers to entry are sufficiently insurmountable and they arise quite independently of the position of the incumbent.

Now, if the Competition Commission's position, as has slowly emerged out of their pleadings, is this U-bend point - you suppress the incumbent and it somehow psychologically encourages new entry - one would expect to see that properly analysed. It is not. One sees analysis of everything which points at the opposite direction, but not at that. Who knows? In theory, it might be true, but it is not something the Competition Commission has investigated, nor analysed, nor reported upon in the report.

PROFESSOR PICKERING: so, your attack is on what the Competition Commission has, or has not, done - rather on an alternative analysis of the market and what might actually happen.

MR. GREEN: That is the case in any judicial review. The decision-maker is certainly not entitled to pull itself up by its boot straps in post-decision pleadings in order to try and justify its decision. One of the reasons that that is extremely important in this context is because if that now is the Competition Commission's theory, it would have consulted very broadly and very widely with the industry, including with the grocery retailers, on that particular option. It would have then set out its conclusions on that option in the report.

The *Interbrew* case was a case where, in relation to a fairly minor aspect of a remedy in relation to a merger, failure to put a point to the industry was held to sound in judicial review. It is why the process is so important. These things are not done by a side wind or by a side glance, or a nod in a particular direction. They are done head-on in a major way, thoroughly, and comprehensively. If they can point to detailed analysis in the report which addresses what I call the U-bend point, then so be it. But, they cannot do. The nearest you can get is a half-line here, and a half-line there from which they extrapolate. That just is not good enough - nowhere near good enough.

PROFESSOR PICKERING: Thank you.

MR. GREEN: Of course, just think of the consequences of para. 102. If they are right - that they cannot analyse these things - how can they possibly come up with the U-bend point? It is inconsistent. If you do not know when someone will enter - and it is impossible to do that - and it is speculative, then how can you possibly say that squashing the incumbent will

encourage the new entry? I mean, that is the benefit point. The U-bend point is a leap into theory on the basis of something they say they cannot investigate.

In relation to the 'It is too hard' point -- Because it would require a very detailed criss-crossing backwards and forwards in the report, we have produced a schedule of the paragraphs that we rely upon. If I could hand that up please? (Same handed)

THE PRESIDENT: Mr. Green, this is in relation to ----?

MR. GREEN: This is in relation to the next point beyond, as it were, the law, which is that they have actually analysed all the points they say they cannot analyse.

THE PRESIDENT: Yes. Yes. You say that actually it is feasible.

MR. GREEN: We say that not only is it feasible, but -- We are not putting forward to you new evidence from any extraneous source to say it can be done. We have simply concentrated on what they did do in the report.

Now, in this schedule you will recollect -- and it is not necessary to go back to it, but in para. 102 of the defence, the Competition Commission says that they cannot make any assessment as to who might enter a market, or where, or when, or in what order. To demonstrate the futility of this assertion we have reviewed the final report and we have put together this schedule of the evidence which the Commission refers to and relies upon in order to found a conclusion. So this is evidence which they, themselves, have found to be sufficiently robust to draw some form of a conclusion on, and it demonstrates they had all the evidence they needed to perform some form of – and I use this word advisedly – "adequate" assessment.

We have done this under a number of headings and the broad headings are the number of of new developments per annum, the percentage of new developments that would be blocked by the competition test, the excess profits that would cease to be made following entry of arrival and the extent to which entry would be delayed, and therefore the persistence of excess profits before the remedy bit. We have set out the various parts of the report that we rely upon.

I would like to pick up, and if I may I would like to do this in conjunction with the Report, some headline paragraphs. These paragraphs demonstrate that the precise activities the Competition Commission said it could not do were, in fact, done. Could I start with p.425 of the Competition Commission Report, appendix 7.3.

I think, Chairman, I should say I think I am going to be finished by about 12 o'clock. One of the reasons I have produced the schedule is to speed up what would otherwise have been quite a slow process.

THE PRESIDENT: I think what we will probably do then is just have a short break, if you keep to that sort of time.

MR. GREEN: Page 427, appendix 7.3, headed "Land controlled by grocery retailers", that describes the purpose for which the Competition Commission collected this information, and I want to go straight to paras.3 and 4, which describe information that they had in their possession. They say:

> "We collected detailed information from the large grocery retailers on more than 1,300 landsites across the UK. This included the location, the size and a detailed history of each site. We commissioned CACI to map the proximity of each of these sites to all of the stores in the local area using their drive-time system (see Appendix 3.2 for further details). Since we have been concerned to ensure consistency in the application of drive-times, both across different local areas and between different retailers, we have used these CACI drive-times throughout all the empirical analysis in this market investigation.
>
> Over the course of this investigation we continually updated and added to our dataset with new information both from the retailers themselves and from submissions and complaints that we received from other interested parties. For those sites that were of particular interest we met twice with each of the four largest grocery retailers to discuss, on a case-by-case basis, the latest information on the site, the history of the site, the future plans for the site and the local context and rationale for the retailer's interest in each site."

If you turn over for the next 60 or 70 pages there is a great deal of information which reflects that.

What we see in relation to land controlled by grocery retailers is that they collected detailed information for more than 1,300 sites, they got the detailed history of each site, they used the third party, CACI, to conduct an analysis, they maintained a dataset which they updated frequently, they then met in relation to those areas of particular interest with each major retailer twice, they conducted case by case assessments, they examined the history of each site, they examined the local context and they considered each retailer's strategic interest in the site. This is exactly the sort of information and the sort of process of information analysis that they say it is impossible to do.

If one jumps back to appendix 7.1 on p.412, one sees another category of information that the Competition Commission had in its possession. This is in appendix 7.1, which is the persistence analysis.

THE PRESIDENT: This is all in your hand-out 2, is it?

MR. GREEN: Yes, it is.

THE PRESIDENT: Just so I know I do not have to take a note.

MR. GREEN: Paragraph 11, p.412:

> "Finally, we identified persisting monopoly and duopoly stores where we have some indication from the main parties that entry may occur in the near future (or since our data was compiled)."

So these conclusions are based upon information as to indications of entry in the near future.

> "We find that that of the 51 monopolies greater than 1,400 sq metres, 40 have no indication of imminent entry whilst 9 indicate one additional competitor is imminent and 2 indicate two additional competitors are imminent in the near future. Of the 67 duopolies, 53 have no indication of future entry and 14 do. In total, we observe that 79 per cent (93 stores out of 118) of persisting monopolies and duopolies larger than 1,400 sq metres have no indications of new store entry in the near future. We also find that of the 25 possible future entries, 14 are due to occur within 15 minutes of stores which we would discount on the basis of insufficient population if we were to apply the 95 per cent population threshold."

So in relation to the key areas they had identified who was going to enter and when. The Competition Commission say they have no ability to identify the sequence or order of entry into a particular market. They examined that. They examined to a degree that they were able to draw conclusions.

In relation to that same matter, or related matter, if one turns back a page to 7.1, para.7:

> "We also find that of the 160 persisting monopolies and duopolies over 600 sq metres, 118 have a net sales area greater than 1,400 sq metres, and of these 11 have another store operated by the same grocery retailer within the isochrone and 36 have applied for or completed an extension since 2000. These vary in size but on average increase sales area by approximately 630 sq metres."

So they had all the historical data in the highly concentrated areas or markets as to who had applied for what and when and what the size and scale of the application was. So they had all the historical data, they had all the present data and they had a certain amount of future data based upon area. The mere fact that we are talking about a fairly sizeable exercise is an irrelevance because the annex demonstrates that they are perfectly able to conduct an

analysis over 1,300 sites, though the total number of sites which are concentrated is very much smaller, of course.

So the scale is not a problem, the data is not a problem. They had a vast lake of data about planning and everything to do with it, and they had it on a dynamic basis – in other words, strategic plans and rationales.

The effectiveness of the remedy will also be affected by the extent to which an area is populated by a monopolist. I can deal with the point that Professor Pickering raised a little while ago, I would just like to show the evidence in annex 6.1 which addresses the question of the extent of monopoly areas. I can do this very briefly.

THE PRESIDENT: Are you still on your hand-out, or not?

MR. GREEN: This is a slight digression. While I am on it, I am just going to provide Professor Pickering with the background data. It is p.384, and I am going to do this quite briefly, and I will give you references as I go along.

Table 1 demonstrates that 386 stores in a 10 minute isochrone were monopolies, this is out of a total of 495 concentrated areas in 10 minute isochrone – you get that from table 3.

One also gets the fact that 209 concentrated areas were within a 15 minute isochrone.

What table 1 demonstrates is that of the 74 per cent of the areas where monopoly areas, that is 368 out of 495 and that figure of 74 per cent reduces to 62 per cent, in other words 130 out of 209 in 15 minute isochrone analysis, and I whizzed over that. The basic figures are 74 per cent reducing to 62 per cent depending on whether it is a 10 minute or a 15 minute isochrone.

The simple point that comes out of that ----

THE PRESIDENT: Where do you get the 495 from? 368 out of 495 you said – I think you might have mentioned where you got it from.

MR. MATHER: Table 3.

THE PRESIDENT: Thank you.

MR. GREEN: If it is helpful, I could put these figures in a short note, it will be on the transcript but if it would help at some point we will spell it out a little bit. It is fairly clear once one works one's way through these figure that the effectiveness of the remedy is going to be affected by the extent to which an area is populated by a monopolist. You are suppressing the incumbent. If you have only one incumbent, then there is nobody else who is an incumbent who can take up the slack demand ----

THE PRESIDENT: They cannot extend their store.

MR. GREEN: Precisely.

MR GREEN: So an indication of the effectiveness, or ineffectiveness of the competition test is going to be the number of incumbents who can take up the slack demand, particularly if the level of new demand falls short of that justifying a new entrant – I gave you the data on that yesterday, and appendix 6 addresses that issue. That is a slight digression, but it does demonstrate that even that level of analysis was available to the Competition Commission one can deduce from that they very easily can work out levels of effectiveness in different scenarios – for example, if you have a monopoly scenario what will be the impact of the remedy. It gives you information from which the Competition Commission can deduce consequences, it goes to scenario analysis, sensitivity analysis which they simply did not do.

Again, I do not want to take up time because I have a few minutes of other matters that I do wish to deal with ----

THE PRESIDENT: Well this is very important, Mr. Green, so do not feel you need to rush it.

MR. GREEN: Can I just take you through this schedule, because I think it is important that you see the structure of it and perhaps the detail can be left to be read, because it is largely self-evident. We have put the references under a number of headings. First, the number of new developments per year (p.3) and the information which was available to the Competition Commission is referred to here. The Competition Commission had available to it the number of planning applications for new stores and extensions, larger than 1000 sq. metres over the period of 2000 to 2004 by the large four retailers. They use this information to estimate numbers of such applications for all stores that would result in the future if the competition test were introduced. We have given a reference to the paragraph numbers and we have said in terms of relevance that the figure could have been used to estimate the likely number of developments per year for the purpose of assessing the future benefits of the test.

The next section concerns the proportion of developments that would be blocked and we referred to the fact that they had a very great deal of information; I have just taken you to some of those paragraphs.

THE PRESIDENT: … that was the 24 per cent figure.

MR. GREEN: They had the 24 per cent figure, that is right, and we have referred to the 24 per cent figure on p.5, but we have given a more detailed analysis of some of the implications that might be drawn from this data in the right hand column, over and above the 24 per cent. The short point is that there was a huge amount of information from which they could assess precisely the things in para. 102 they say it would have been too speculative to

address as a justification for not having performed the exercise. We have pointed out on p.3 that they were able to identify in numerical terms, or approximate numerical terms and percentage terms the number of stores that would not be able to extend with the competition test set at 60 per cent. We have referred in the box below that to the fact that the Competition Commission had information on the number of planned developments for new stores and extensions that Tesco considered would fail the competition assessment. Now, we are fairly certain that the Competition Commission had equivalent information from all other major retailers but they had individual plans from each retailer. Again, the information I have already shown you indicates that that must be the case. They had information because they needed it to calculate the AEC, or to estimate the AEC on the excess profits that were made and would cease to be made following the entry of a competitor assuming that every blocked development would be replaced by a rival development – we are given the information on p.6.

Then we have addressed the question of the amount of time that might occur in relation to any new entrant in para.7, which is on pp. 6 and 7, and there is quite a lot of that.

There are not that many blocks of information that one needs in order to assess the benefit of the competition test, and *a fortiori* the dis-benefit, the cost. It is a fairly simple point, the difference between the two parties is quite stark. They say they could not do it; we say on the basis of findings that you made and the evidence you refer to you had sufficient to perform an appropriate assessment – we do not say necessarily that the Competition Commission could have examined it and come up with a precise quantification, but they could do it to a sufficient degree of accuracy, avoiding spurious accuracy. So their justification for not performing the exercise is one we say if correct (i) rebounds upon them in law, but (ii) is not a rational or justifiable excuse for the omission. The exercise is simply the corollary of measuring or estimating the AEC which they did to, in their own eyes, a reasonable degree of accuracy.

Can I move to two final points and then draw some short conclusions? First, the Competition Commission's point that they are not required to conduct the cost benefit analysis. I have taken you at some length to what we say is meant by "cost benefit analysis". It is not a term which is a principle of law, we have set out what we believe is the principle of law, which are those tests applied under s.134, so I am not going to go over that again, but I would like to pick up points in their skeleton argument, particularly paras. 30, 32 and 61 which we say demonstrates a fairly profound confusion in their thought process.

First, para.32 the Competition Commission says:

"The assessment required of the Commission is not a CBA." We simply say the assessment required is that under s.134, we submit that at various points in those questions they are required to assess the costs and measure them, and if the Competition Commission is here saying that they are not required to take any account of the costs then we submit they have erred in law. If that is their case it is hard to see how that is consistent with paragraph 50 where they say they have to take account of the costs. They say:

> "The Commission does consider the relationship between ends and means, but it is not engaged in simply trying to calculate the net benefit of doing X versus not doing X."

Again, if what they are saying is they do not engage in that analysis at all we say they have erred in law, it is not clear absolutely whether they are saying they have got to do it or they have not. They said:

> "Instead, the mandated statutory objective – a comprehensive solution to the identified AEC or customer detriments – is the principal focus …"

Pausing there, they appear to be suggesting that they must achieve a comprehensive solution. If that is their position it is wrong in law. They are required to have regard to the need to achieve a comprehensive solution. It is mandated only in the sense it is something they must have regard to, it does not constitute a test which they apply which leads them to a result. They are entitled under the Act to ignore it having had regard to it if that is appropriate.

Then they say:

> "-- where it has determined what remedy or combination of remedies would provide such a solution, the initial focus of the proportionality exercise is to consider the burden of that remedy in the context of the AEC or consumer detriment that is being addressed".

Well, they plainly accept proportionality as relevant. In the concept of a burden, since we say that costs arising out of the competition test will exacerbate the AEC for reasons that I have explained, then we would assume that both here and in the context of para. 50 of their skeleton, they accept they should have taken account of the costs. Then they say,

> "However, if the Commission considers that there are alternative remedies that would provide a solution, it must consider the comparative costs of those alternatives and choose the less (or least) onerous".

Well, we would not quibble with that as a basic proposition.

Tracking back to para. 30,

> "In none of the authorities on the general principle of proportionality is there any requirement for a cost benefit analysis as regards a particular measure or remedy. This would not only a place a broad and flexible doctrine within an unacceptable straight-jacket, but it would focus narrowly on the particular consequences of the remedy and not the objective or the concern at which the measure is addressed".

Again, if - and one has to preface almost all these sentences with an 'if' -- If what is being suggested is that they do not conduct any cost benefit analysis, we say they have erred. If they say, "Yes, we conduct a cost benefit analysis in the broad sense in which we have described as part of the process", then one could not quibble with that. They then say,

> "In some cases, it may be altogether reasonable for a measure to have financial implications for those on whom it is imposed, but on no less than the benefit produced by that measure in alleviating the detriment to the public at large".

That is an important sentence because it is an implicit recognition that if a remedy imposes costs you must measure them against the benefits. What they are saying is that if the costs are equal to the benefits, then it may still be appropriate to impose the remedy. In the present case they have not analysed the costs and they seem to suggest that they did not have to. We think this is an implicit admission that the costs have to be taken into account and measured - again, I preface it - in an appropriate way to the benefits. They then say, "This will depend on the statutory context and framework".

Then, finally, at para. 61, they submit that Tesco's approach is wrong in principle. I should say that the bit that I object to is the last part of this paragraph, but I will read the whole paragraph,

> "Tesco's approach is wrong in principle. Tesco seeks to argue that because the Commission considered only 'on balance' that its conclusion was robust, that margin should somehow be factored into the formulation of the remedy. That is to say, suppose the Commission was only 70 percent sure that a customer detriment was created, it should modify or temper any remedy to discount for the possibility that it might be wrong. But that is not at all what the Commission is required to do. It is required by statute to decide whether certain effects occur on a market (ss.134(1) to (2))".

Now, that is not relevant to the point I am making now. That is the AEC question. "It makes that decision on the balance of probabilities and it is not suggested that the Commission should apply any higher test".

Then one gets down to remedies.

> "Once it has so decided that there is an AEC, it may consider whether there is any resulting effect on customers but must in any event decide upon as comprehensive a remedy to that AEC or any resulting from the customer detriment as is reasonable and practicable".

Now, we understand this to indicate the following: that they view it as mandatory to apply a comprehensiveness test. We submit that is manifestly wrong in law because if that is what is being suggested it is inconsistent with the language of the Act which says that you simply take it into account. There is a clear difference between being required to apply comprehensiveness as a test and taking it into account. The latter contemplates that having taken it into account, you are entitled to ignore it in an appropriate case. But, if you have to apply a comprehensive remedy, then statute and parliament compels that you do that. So, they are subtly, but importantly, different. The words must, in any event, seem to infer to us a legal error. Indeed, the permissive word 'may' in the line above - "Once it has so decided there is an AEC it may consider whether there is any resulting effect on customers ---" if they are simply saying, "They are permitted to do that, but need not", we again submit that that is an error of law because they are required to consider practicability, reasonableness (i.e. proportionality) as well as comprehensiveness, and those do require them to take account of costs and benefits as elsewhere they seem to accept.

THE PRESIDENT: We really have to focus on what they did, do we not? This is a gloss, obviously, by way of an argument ----

MR. GREEN: It may be. We have looked to see whether or not there is any analysis in the report - in particular of the 'whether or not'. They address remedies at some length. In terms of this fundamental question we say they have to pose - should they impose any remedy at all - one would have expected to see a section, "Should we impose any remedy at all?" as opposed to, "We have identified an AEC. We must now impose a remedy". That is Question 2 as opposed to Question 1 in remedies. It seems to us that they leapt over Question 1, and they did not pose it, and they did not answer it in the report. They did not ask themselves, "Should we adopt any remedy at all?" They did freely accept -- decide, for example, that they would not impose divestiture and they would impose this competition test. But, that is Question 2: "If we impose a remedy, which one?" But, that *a priori* question, "Shall we impose any remedy at all?" does not appear to have been either posed, nor answered in any material or cogent manner at all.

MR. MATHER: I am just thinking aloud: Is it material in this case because you do not attack all their remedies. You only attack the competition test. So, you are not suggesting that if they had posed the question that you say they should have posed, they would probably have come up with the answer, "Well, there's no remedy needed at all".

MR. GREEN: They have to ask themselves whether to impose the competition test at all. Now, that may come under Question 1 or Question 2. So, in relation to each remedy, you are going to ask yourself, "Shall we impose any remedies? If we impose a remedy, which of the remedies?" You have to ask yourself in relation to each one of those, "Am I entitled to impose the competition test? Is it proportionate, practicable, comprehensive?" So, the *a priori* question will arise both under Question 1 and Question 2. We are only concerned here with the competition test - not with the restrictive covenants part of that.

Very finally, just drawing some conclusions together, we submit that the Competition Commission did not assess the benefit - in other words, the extent to which the competition test would address the AEC. We submit that in the absence of this analysis none of the relevant questions can be answered, either at all, but certainly not against the companies who might be subject to a remedy. We submit that if they are right in 102 - that is the legal consequence which follows - then we submit that in any event they erred in their analysis of the approach to be adopted because they decided only that they could not quantify it, but they did not move down the scale of analytical techniques that were available to them.

That, we say, is an error of law. Albeit that it flows out of guidance, we believe these are sufficiently established principles - or should become so - that a regulator engaged in such a detailed exercise, with such evidence in front of it, should have, in applying the test under s.134, worked its way through that scale of analytical techniques. We do submit that it is wrong in law not to have done so, and to have drawn the shutters down at, "It is all just too difficult".

Further, we submit that they erred because on the basis of their own finding and their own conclusions they did have evidence upon which it was sufficient to draw appropriate conclusions. That is our schedule.

Finally, that these failures were all the more serious because the Competition Commission itself identified that its own remedy created a risk of exacerbating the AEC. That is, as it were, Ground 1. But, in circumstances where there is that risk it imposes an even more acute responsibility or duty on the decision-maker to perform an adequate exercise. You know there are dis-benefits, and it is even more crucial that you engage in an assessment of the benefits because there is at least a risk that the dis-benefits may outweigh the benefits.

MR. MATHER: So, you say that sort of highlights the need to assess the benefits.

MR. GREEN: Yes. It is an important point because the dis-benefits and the benefits focus on precisely the same thing, which is the AEC. You are comparing apples with apples. The disbenefit means that monopoly power will persist longer because the person most likely to meet that demand is suppressed. If you have got high barriers to entry statistically, inevitably, because you have taken one person out of the pool of potential meeters of demand, you have increased the risk that the AEC persists for longer. So it addresses the same issue, and that is the only point I am trying to make here. It addresses the AEC, whether you are looking at cost or benefit, and that is why it should have been a relevant consideration at stage two as well. It impacts upon benefit.

Those are our submissions. Everything else which we have set out in the skeleton, points of detail, we leave to be addressed there. We certainly do not resile from them. What we have sought to do in our oral submissions is focus on the main points, in particular dealing with the points as they have emerged from the Competition Commission's analysis and in its skeleton argument, and its defence. We thought that we did address those, but we certainly do not resile from our complaints that much of the Competition Commission's reasoning as it has emerged in the pleadings is new after the event boot-strapping. In principle and in administrative law, we say they are not entitled to do that. If these are serious issues they should have formed a very major part of the investigation and the conclusions, but we nonetheless have addressed them.

Unless I can assist further at this stage, those are our submissions.

MR. MATHER: Just one very brief question, if I might, it was your fourth point about the CBAs coming out of guidance and you said these are sufficiently established or should become so, etc. Can you help me, is there is a difference in law between those statements so far as we are concerned between whether they are sufficiently established by authorities or precedent or whatever, and should become so, which suggests that we might be being asked innovate.

MR. GREEN: I put it in those terms deliberately as, in effect, an invitation. We do believe that the principles should be common sense principles of good regulation, and in the context of competition law should be imposed upon a decision maker. They are not unduly onerous or unreasonable, they are common sense and we think they flow out of s.134. We pointed to the guidance of this Tribunal in relation to the *GEMA* decision, the Competition Commission's own guidance, Ofcom, the Green Book, in order to demonstrate that they are common sense principles. If you conclude that the practice has got to this level but

ought to incrementally rise another few inches to become a point of law we invite you to say so, that this is an error on their part if they fail to apply these tests. We believe in the context of the competition law it is an error of law.

THE PRESIDENT: This is all under the heading, as I understand it, of proportionality. These are elements, are they not, of what applying proportionality principles means in practice in these sorts of cases?

MR. GREEN: That is right.

THE PRESIDENT: Do you put it any higher than that?

MR. GREEN: No, that is why I say it comes under the rubric of s.134, because that is the statutory framework, we are bound by it, the Tribunal is bound by it. We have to work out what that means. Reasonableness imports proportionality, we agree on that, and these are simply ways in which one applies a proportionality or reasonableness test.

THE PRESIDENT: Then there is a double-proportionality issue, proportionality overlaid on proportionality. To see how much of an analysis you need to go into you also have to apply proportionality.

MR. GREEN: Yes.

PROFESSOR PICKERING: Mr. Green, just one further question. About unmet demand and that concept and the concept of need is obviously related to it, I wonder whether you could comment on the extent to which that notion of unmet demand, as used, as I understand it, by planners, has any bearing or relationship to the way in which your clients or other retail businesses would actually identify capacity constraints and indeed the problem of excess demand. It seems to me, just to explain why I am asking this, that we do not have a London airport situation where the argument about an extra runway is that we are using 103 per cent of the capacity, because in retailing I am not sure that all the check-outs are ever in use and the car parks are full, and so on. How does business relate to the planners' approach on this?

MR. GREEN: I think there are a number of points to be made. The first point is that the Competition Commission looked at planning need as a proxy for unmet demand. It is set out in appendix 7.2, p.422 of the Report, what "need" meant in terms of a planner's conception of word. The Competition Commission was only examining need in this context because it was an indication of the extent of unmet demand. The Competition Commission, itself, viewed it as a reasonable proxy. I plainly accept the premise that it has been performed by the local planning authorities for a different purpose. The test which is referred to in paras.12 to 14 of appendix 7.1 explains what is meant by "need", and I think

it is a reasonable proxy. I use the word "reasonable", but it is a proxy for a form of unmet demand.

MR. ROTH: Just to be clear, I think Mr. Green is referring to appendix 7.2 not 7.1.

MR. GREEN: Yes, sorry, 7.2, p.422.

THE PRESIDENT: Page 422, "Requirement to demonstrate 'need'"?

MR. GREEN: That is right, it is in a section entitled "The planning framework and grocery retailing", p.419.

MR. ROTH: Yes, that appendix, as it states at the beginning, is just attempting to set out the law on policy relating to planning, it is not drawing any conclusions.

PROFESSOR PICKERING: Do we look somewhere else for ----

MR. GREEN: I think I gave you the paragraphs. I think I took you to the paragraphs in the Report yesterday which deal with this, and I can try and find those again. This was simply one source of information. The other sources of information were the population analysis and the persistence analysis. Those were the two principal sources that the Competition Commission examined in order to identify the existence of unmet demand. They looked at a variety of sources. So the persistence analysis enabled them to form some strong conclusions. The population analysis likewise was consistent and they looked at planning need. Mr. Roth is absolutely right, they were describing in this section just the planning requirements, but they also were able to identify that there was considerable need. I think the paragraphs are 7.36 to 7.41. This under the heading "Planning rules and their impact on entry and expansion", so it is not just a description of the planning regime, it is an analysis of the impact of the regime on the market. 7.41:

> "Our own survey of LPAs indicated that 62 per cent had quantified a need for additional floorspace for the retailing of convenience goods (ie consumer goods purchased on a regular basis, including food, toiletries and cleaning products) in their local development plan."

They then identify the average need as 4,600, median 2,500. They then say:

> "The majority of the LPAs that did not have an identified need … were those that did not have an up-to-date development plan."

I think they are suggesting that had they had an up to date plan the position might have been different. Then they indicate that a small percentage, albeit a significant minority, had up to date retail development plans, and concluded they did not have a need. So a high percentage had identified a significant need. This was in the section assessing the impact of planning, and it is a fact which informs their analysis of barriers to entry.

PROFESSOR PICKERING: But it influences the planners, and we understand that the Competition Commission in its Report has latched on to this. What I am interested to know, almost in a word, not only from you but maybe from the Interveners as well in due course, is whether that concept – apart from affecting attitudes to planning applications has any bearing on business decisions about use or development or expansions?

MR. GREEN: There is evidence in the report to the effect that a number of retailers made detailed submissions on whether the need requirement should be abolished. I am not certain how much of that actually feeds in detail. We have looked at it for the purposes of this appeal but not all of it actually feeds into the report. If one opens that particular can of works one will find that a lot of information from each retailer as to that particular issue – various retailers did have different views on it. We can certainly provide you with some information. We would need to go back and get what was said about it if that would be of assistance; I am not certain it is sensible to do it at this point.

PROFESSOR PICKERING: Sure, okay

THE PRESIDENT: It may be that with the local retail development plans the input is from retailers. It may be that LPAs arrive at their retail development plans having surveyed the local retailers' intentions ----

MR. GREEN: That is why I was drawing your attention to appendix 7.2, because it explains the information that an LPA will have in order to identify need.

PROFESSOR PICKERING: Part of that need, of course, is the opportunity to generate local tax income, is it not, from the development of business premises?

MR. GREEN: I could not possibly comment on that one! I do not recollect it as something the Competition Commission has made a finding about, but certainly one of the matters which the LPAs and the Competition Commission acknowledge were relevant to the assessment of need were the quantitative demand for floor space; in other words, the extent to which demand exceeded supply. That is explained in paras. 12 to 14 of appendix 7.2 and that is why unmet demand is plainly part of the LPAs need assessment, but I absolutely accept it is within a different context, but the Competition Commission looked at it as part and parcel of its analysis.

THE PRESIDENT: Shall we just take a very short break, although we are going to stop at 1 o'clock anyway – have you finished now?

MR. GREEN: Yes, I have, thank you very much.

THE PRESIDENT: Shortly after half past 12.

(Short break)

THE PRESIDENT: I am sorry, Mr. Roth. Mr. Green, I meant to say this before, but we have oceans of economic evidence and you have not said much about this at the moment. It may be that you are going to say it is not relevant, and we need not trouble ourselves with any of that; that is fine if that is the case.

Secondly, there is the way that the matter was argued in the skeleton was more of a point about the quality of the AEC and the uncertainty and that one should feed that into the proportionality analysis. That is not quite the point you have been making, which was rather different and really saying that it is feasible and so on, but it is not the uncertainty point. Is that something which you are now 'soft-pedalling' as it were? Do we need to worry ourselves about ----

MR. GREEN: Can I deal with first of all economic evidence? We do not accept the criticisms made of our experts, we responded to the Competition Commission's, but it does seem to us that the points which the economists make are points which find reflection in the Report and the easiest way to resolve that is to take one's inspiration from the report, stick to the Report, point out to you what is in the Report, so at the end of the day the points we have made in the skeleton flowing from the economist's report we believe stand, but our case is certainly not dependent on them, they are extra detail, extra support for points which flow out of the Report which is why I have not felt it necessary to go into that, it is just not necessary to address it. If you, the Tribunal, take the same view then what is stated by the economists comes out as argument and is found in the Report.

So far as the quality of the AEC is concerned this is an issue which we are content to leave on the skeleton, we do not resile from it, it is a relatively small point relative to the two big points that we have made, and we are happy to leave it on the skeleton. We accept the point made by the Competition Commission that the basic test is to be determined by 51 per cent – civil standard of proof – but we do not think that is the answer. In terms of proportionality you should measure the strength of your conclusion about a particular finding.

So far as the AEC is concerned, you have seen that they have set out estimates, they have set out parameters and so on and so forth. So far as the benefit is concerned, we have seen what their assessment is so far as the cost is concerned, and we simply think that one part of the proportionality test is to wave the confidence that you have in any particular finding – what we have loosely described as the "robustness", it simply goes into the proportionality test.

Now, as you have seen there are a number of disputes between economists on this, but I have not thought it necessary to take up what would have otherwise been quite a lot of time dealing with that, we think it is a short point; in reality it is essentially a legal point and we are happy to leave it at that.

THE PRESIDENT: Right, thank you. Mr. Roth?

MR. ROTH: Members of the Tribunal, I am sorry to start on a gloomy note, but I am beginning, of course, rather later than the 11.30 that was anticipated, and that is no criticism, I am not making that as a criticism of Mr. Green, it is a fact. It means that I fear I am most unlikely to finish today -----

THE PRESIDENT: Shall we sit at 10 tomorrow?

MR. ROTH: It may be sensible to make arrangements to sit at 10 if that is not an inconvenience. I thought I would mention that straight away.

This is an application for Judicial Review of a small part of a very large and comprehensive investigation by the Competition Commission. It is, of course, a Judicial Review and not an appeal – a point that I know this Tribunal will have well in mind since you have so recently had to advert to it in the Tribunal's judgment in the *BSkyB* which we refer to in our skeleton.

Mr. Green has now, in his oral submissions and as has just been pointed out in a question from the Chairman – very much in contrast to the notice of application and the written submissions and indeed the witness statements that Tesco put in – based himself very firmly on the findings in the Report, and he has certainly not developed any challenge to the accuracy of the findings of detriment from the AEC which the Commission made. Indeed, he sought to rely on them a short while ago saying "Look how estimates can be carried out", and he has certainly not developed any challenge to the robustness of those findings, although he said he does not resile from what is in the skeleton, but of course one of the findings of the Commission is that the margin concentration analysis, which was the focus of so much of that written material, was sufficiently robust, and that is a finding that they made.

Moreover, in our submission it is necessary to have regard not only to the nature of the challenge that this is a Judicial Review, but also the scope of the challenge and, as the Tribunal knows, the Commission was rather concerned at the outset by the rather vague relief that was sought in the notice of application – the paragraph at the end saying what actually Tesco is seeking to quash, and what Tesco is asking the Tribunal to do. So the Commission wrote back in July to Tesco's solicitors to ask exactly which parts of the

Report are being challenged? The answer, if I could just take you to that, is in Bundle 5 - the letter of 11th July (in answer to the letter of 4th July). In the second paragraph,

> "It is precisely because of the length and nature of the Report that the formulation at para. 31 of notice of application takes the form that it does. It order to assist both the Competition Commission and the Tribunal, we confirm that we seek an order quashing para. 43 of the Summary and paras. 11.12 to 11.16 and paras. 11.437 to 11.441 of the Report, i.e. those parts of the Report which set out the remedies relating to 'Planning and the competition test. However, we reserve the right to make further submissions on the appropriate scope of relief at any stage in the proceedings, in particular following the substantive judgment of the Tribunal".

I ask you to note that because I will return to it.

The starting point, of course, is the statutory exercise which the Commission has to carry out under the Enterprise Act. There was some discussion of the inter-relation between ss. 134 and 138 early on in Mr. Green's submission. I did, at first, think that might be, though interesting, somewhat academic for this case, particularly given the extent of the AEC that is found. I do not think Tesco is suggesting that there should have been no remedy - the controlled land sites remedy is not being challenged.

However, today, Mr. Green returned to that in making his submissions and says, on one approach, "Well, we were not entitled to adopt the competition test because the Commission approach wrongly the requirements of a comprehensive solution under the statute". You will recall the submission a short while ago. It really goes to the adoption of the test at all. So, I think this has become important and it may be helpful to explain how the Commission understands the governing provisions of the statute and the duty which it is under.

May I ask you to take the statute either in the Purple Book at p.235 or in the authorities' bundle? It is s..134(1),

> "The Commission shall, on a market investigation reference, decide whether any feature, or combination of features, of each relevant market prevents, restricts or distorts competition ---"

I need not read the rest. Sub-section (2) defines that as being an adverse effect on competition, or an AEC. So, the first question which the Commission must answer is: Is there an AEC? If there is none, that is the end of it. That, I think, is common ground. If the answer is, 'Yes, there is', then one moves to sub-section (4),

"The Commission shall, if it has decided on a market investigation reference that there is an adverse effect on competition, decide the following additional questions".

Then one has sub-paragraphs (a), (b),and (c).

"(a) whether action should be taken by it under s.138 for the purpose of remedying, mitigating or preventing the adverse effect on competition concerned or any detrimental effect on customers so far as it has resulted from, or may be expected to result from the adverse effect on competition;

(b) whether it should recommend the taking of action by others for the purpose of remedying, mitigating or preventing the adverse effect on competition concerned or any detrimental effect on customers so far as it has resulted from, or may be expected to result from, the adverse effect on competition; and

(c) in either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented".

Sub-section (4) which I have just read is to be read with sub-section (6) just below. "In deciding the questions mentioned in sub-section (4), the Commission shall, in particular, have regard to the need to achieve as comprehensive a solution as is reasonable and practicable to the adverse effect on competition and any detrimental effects on customers so far as resulting from the adverse effect on competition".

So, in answering the sub-section(4) questions, the Commission must have regard particularly to the need to achieve as comprehensive a solution as is reasonable and practicable. That is the approach it has to take. So, we say having found an AEC it must come and decide upon a remedy, or remedies, unless any possible remedy would be unreasonable or impractical. Mr. Green said that sub-sections (4)(a) and (b) were each sort of discreet binary questions. We say that is a very artificial way of looking at it. The comprehensive solution that the Commission must, in particular, have regard to the need for finding can be found through action by the Commission itself under (a) or maybe in a recommendation for action by others under (b), or a combination of the two (as, indeed, in this case). But, to postulate a situation where the Commission finds an AEC, having regard, as it must, to the need to achieve a comprehensive solution as is reasonable and practicable, but to conclude no action should be taken by it, and no action should be taken by others to be recommended is quite contrary to the whole thrust of this provision. That meshes with s.138.

THE PRESIDENT: You mean it is an impermissible result and it cannot even be conceived of?

MR. ROTH: It can be conceived of theoretically that there is no reasonable or practicable action that can be devised to achieve a comprehensive solution. Yes, theoretically it is possible. It would be a very extreme result. But, the idea suggested this morning, "Well, the Commission just has regard to the need to achieve as comprehensive a solution as is reasonable" and to say, "Well, we have regard to that, but we now ignore it" -- Those were the words Mr. Green used. We say that that is, frankly, preposterous. Of course, that is not what the section is aiming at.

That is how it meshes with s.138. That is in mandatory terms, again subject to reasonableness and practicality. The heading that was referred to, I think, by Mr. Mather is, with respect, very pertinent. As you know, it is a well-established House of Lords authority, and the heading cannot overwrite the language of the section, but it can assist in its interpretation.

In sub-section (2),

> "The Commission shall, in relation to each adverse effect on competition, take such action under s.159 or 161 as it considers to be reasonable and practicable ---"

-- to achieve (a) and (b). Then, sub-section (4) again, the need to achieve as comprehensive a solution as is reasonable and practicable.

There is assistance here that the Tribunal can find from the judgment of this Tribunal in the *Somerfield* case, because although that was a merger case the language of the relevant statutory provisions that fell to be construed is, as you will see, sir, and may indeed recall, exactly the same. The *Somerfield* case is in the authorities' bundle at Tab 8. (Your bundle 23.) . If you could keep the Purple Book out. One can actually take the statutory language in the judgment. If you go to para. 12 of the judgment on p.4, this was a completed merger in the same section, as it happens, that we are concerned with, the same sector, supermarkets.

Paragraph 12 sets out s.35 of the Act, and you will see what the Competition Commission has to do. If you go down to sub-section (3), or you can take it in the Purple Book:

> "The [CC] shall, if it has decided on a reference under section 22 there is an anti-competitive outcome (within the meaning given by subsection 2(a)), decide the following additional questions –
>
> (a) whether action should be taken by it under s.41(2) for the purpose of remedying, mitigating or preventing …"

- in this case it is the SLC –

"… concerned or any adverse effect which has resulted from, the substantial lessening of competition;

(b) whether it should recommend the taking of action by others for the purpose of remedying, mitigating or preventing the substantial lessening of competition concerned; and

(c) in either case, if action should be taken, what action should be taken and what is to be remedied, mitigated or prevented."

Then if you look across to para.15:

"As to remedial action, section 41 of the Act provides …

(2) The [CC] shall take such action under section 82 or 84 as it considers to be reasonable and practicable –

(a) to remedy, mitigate or prevent the substantial lessening of competition concerned; and

(b) to remedy, mitigate or prevent any adverse effects which have resulted from, or may be expected to result from, the substantial lessening of competition."

There is an exact parallel with 35 and 41 on the merger part of the Act and s.134 and 138 of the market investigation section, one which mirrors. The heading of s.41 is "Duty to remedy effects of completed or anticipated mergers", again, rather like s.138, "Duty to remedy adverse effects". The heading is not reproduced in the judgment, but it is in the Purple Book.

Those were considered by this Tribunal in the judgment. If you turn, please, to p.33 in the judgment under the sub-heading "*The CC statutory powers*", para.86:

"We begin with the CC's statutory powers, set out in section II above. It is not contested in the present case that Somerfield's acquisition of the disputed stores gave rise to an anti-competitive outcome, within the meaning of section 35(2)(a) of the Act, by virtue of the SLC thereby created. It follows, in our view, that the SLC in question was required to be remedied as quickly and effectively as possible.

Having found an anti-competitive outcome under section 35(2)(a), under section 35(3) of the Act, the CC had to decide, notably, what action it should take for 'the purpose of remedying, mitigating or preventing' the SLC it had found. In that regard, under section 35(4), the CC had to have regard to the need to achieve 'as comprehensive a solution as is reasonable and practicable'. Under section 41(2) the CC was required to take such action 'as it considers to be reasonable and

practicable' in order to remedy, mitigate or prevent the SLC in question. Such action includes divestiture, under the combined provisions …"

They go on to say – and it has wider implication for the present case – in para.88:

"It follows in our view that the CC had a clear margin of appreciation to decide what reasonable action was appropriate for remedying, mitigating or preventing the SLC created by Somerfield's acquisition of the disputed stores."

We say that is of considerable assistance when dealing with this question of construction.

PROFESSOR PICKERING: Mr. Roth, the implication of the two "whethers" in 134(4) – let me just clarify – you are leading us to take the view that it would only be in most exceptional circumstances that at least one of those does not lead on to remedial action under 134(6)?

MR. ROTH: In other words, neither of them could apply.

PROFESSOR PICKERING: Neither of them could not apply, as it were?

MR. ROTH: "Neither of them could not apply" – if I have followed the double-negative, yes, it is only in the most exceptional circumstances that the Commission could say, "Having regard, in answering the question, to the need to achieve as comprehensive a solution as is reasonable and practicable, no action should be taken by us, and no action should be recommended to be taken by others".

PROFESSOR PICKERING: So it is not open to the Commission to conclude under 134(6) that it could not achieve a reasonably and practicably comprehensive solution, and therefore that it should not act under 134(4)?

MR. ROTH: It has got to do "as comprehensive a solution as is reasonably practicable", so it may not be comprehensive, but "as comprehensive" – I think I say it is theoretically open. One cannot say that it is theoretically impossible, but the thrust of the section is that that is not the outcome that is expected. The thrust of the section is that you answer those questions either by finding action that the Commission takes itself or recommending action by others or some combination.

PROFESSOR PICKERING: Of course, we do not have at the end of 134(4)(a) "or/and", do we? There is nothing that leads on to (b), whereas there is an "and" at the end of (b).

MR. ROTH: Yes, I think it has to answer all those questions. It has to answer the following questions, if one goes to the governing sentence of sub-section (4).

PROFESSOR PICKERING: They are cumulative questions, are they not?

MR. ROTH: Yes, they are not alternative.

Sir, I know I have only just begun, but ----

THE PRESIDENT: That is probably a convenient moment, is it not?

MR. ROTH: It is probably convenient because I am going to turn to something else.

THE PRESIDENT: Very well, two o'clock then.

(Adjourned for a short time)

THE PRESIDENT: Mr. Roth, on timing we are going to be all right, are we, so far as you are aware, if we start at 10 tomorrow, we do not need to find any other extra time?

MR. ROTH: I very much hope so, perhaps I should answer the question again at 4 o'clock, and I am not sure how long my friends for the three Interveners anticipate being, but yes, I would envisage finishing mid-morning tomorrow, and I hope that will mean there is time for the three Interveners and reply. Mr. Green has had a long development of his submission so I imagine the reply will be rather shorter.

THE PRESIDENT: Anyway, you have given an indication of when you expect to finish, so the others can perhaps have a think about that.

MR. ROTH: I have not spoken to my friends as to how long they intend to be as Interveners, so I cannot fully answer that question.

I was talking before lunch about the Statute in general terms, and the proper interpretation of it and now come to its application in the present case, as regards competition between large grocery stores – or "supermarkets" to use the looser term – where the Commission found that they are in a distinct market and there were features of that market which had an adverse effect on competition, so that was answering the first question under s.134, and that one finds in the Report at paragraph 10.9. Indeed, they refer, at the start of that section at 10.7 under the heading "Features which prevent, restrict or distort competition" they refer to s.134(1), and in 10.9 the Commission says:

> "We find that a combination of one or more of the following features of certain local markets for the supply of groceries by larger grocery stores prevent, restrict or distort competition in connection with the supply of groceries by larger grocery stores in those markets:
>
> (a) A significant number of local markets have high levels of concentration, and these high levels of concentration have in many cases persisted over a number of years.
>
> (b) The planning regime … and its application by Local Planning Authorities in accordance with the policy objectives of the planning regime necessarily act as a barrier to entry or expansion in a significant number of local markets."

- and they explain how.

(c) The control of land by incumbent retailers through land bank sites, restrictive covenants, exclusivity arrangements, and landsites that are leased or sub-leased to third parties in highly-concentrated local markets acts as a barrier to entry, by limiting entrants' access to potential sites for new larger grocery stores."

Then at 10.10 they look at the differently defined market that encompasses mid-sized and larger stores. Then they go on, having found such features to look at the detrimental effects on consumers further down that page. Again, following the Statute – the Statute I think says "detrimental effect on customers" they here use the word "consumers" because the customers in this case of course are consumers. 10.13 they set out the detrimental effect on consumers. 10.14 they give an estimate of magnitude at the local level, and 10.15 at the national level, and 10.16 the supply chain. They say that all of that is sufficient to justify remedial action. Mr. Green read those paragraphs just a few moments ago so I will not read them again. The scale of the detrimental effect they find is significant, indeed, substantial. That is a summary of course of what has gone before in Chapter 6.

They refer, when talking about the planning barrier to entry, necessarily acting as a barrier to entry, and that is a reference to the fact that they found that the barriers to entry from the planning process were necessary and appropriate for the objectives of the planning regime. One sees that if one goes back to their conclusions on barrier to entry at 7.65 to 7.67.

"7.65 In conclusion, the planning system, in pursuing the broad-based objectives for which it is intended, necessarily constrains new entry by larger grocery stores. It also has the effect of increasing the time for new larger grocery store entry to take place due to the need to assemble sites likely to be granted planning permission as well as the time required by LPAs to consider planning applications."

They then talk about the costs and say that means the existing large retailers are better placed than regional retailers and new entrants to the industry. 7.67 is a significant paragraph:

"The planning regime places more limited constraints on the extension of existing stores by grocery retailers compared with new larger grocery store entry. An incumbent grocery retailer, by extending its store, will make new larger grocery store entry by a rival grocery retailer more difficult."

That is an important finding to which I will come back. They also found barriers to entry from controlled landsites and, as you saw from the summary in Chapter 10, controlled

landsites it is not just restrictive covenants, it is a range of measures and agreements that are used by all the large retailers to restrict the use of land for grocery retailing. Controlled landsites is used as a shorthand to cover them all – there is a definition of "controlled landsites" in the glossary at the end, I do not ask you to turn it up but it covers restrictive covenants, exclusivity agreements, landbanks and so on.

So the remedy set out in the report was a package which first of all removed one identified area of barrier to entry namely the controlled landsites that a supermarket could block from rivals. It did not totally remove it with exclusivity agreements, because they saw the benefit from exclusivity agreements, those are the agreements when a developer – say Westfield Shopping Centre developer – makes an agreement with, say, Waitrose. Waitrose will come in but is promised there will be no other supermarket there and we said we can see that encourages entry but limited it to five years. So they removed, curtailed, the barrier to entry on controlled landsites, and secondly, recommended the competition test as part of the planning process with an override, or safety valve, or exception for exceptional cases where there was an identified public benefit for the local area from the development which the local planning authority would have the right to assess. You know of course by now very well the details of the test, the first limb – the fascia count, the second limb – the 60 per cent share of grocery sales' area and there is extensive reasoning in the Report how they got to the fascia count? Why a fascia count included, why at 60 per cent? and so on.

The Commission saw those remedies as bringing twin benefits, and very important that it is twin benefits - first, the prevention of the creation of new areas of high concentration - which in the absence of the test might come into being even though they are not there now; and, secondly, over time (and I will come back to 'over time') existing areas of high concentration would become less concentrated through a process of dynamic competition and rivalry between larger grocery retailers. Certainly they would not become more concentrated.

I would also emphasise at the outset that these findings of adverse effect on competition and the resulting customer detriment, and the adoption of the competition test, were not an anti-Tesco move. There was a lot of criticism by Tesco by various parties in their submissions to the Competition Commission and the Commission was at pains in its report to reject those criticisms. Even on the competition test itself, when coming to design the test, one retailer - I think it was Sainsbury's - said, "Well, there should be a lower threshold for Tesco because Tesco is so big, as opposed to the threshold for everybody else". It is 60 percent for everybody else and I think they said 50 percent for Tesco. The Commission

said, “No, we are not going to do that. This test is designed to address a feature of the market - high concentration that arises from the way the market has worked - and not from Tesco’s activity. It should apply to all large grocery retailers, irrespective of their identity”. That is in the report at 11.68. It was Sainsbury’s. “Sainsbury’s proposed that the local market share threshold above which a grocery retailer should not be able to operate from a new development should be more stringent for a retailer with national market power. Sainsbury’s said that Tesco’s share of national sales, and its purchasing cost advantage, often combined with high local market share, meant that it could afford to bid more for new space than its competitors. It also said that Tesco had a greater incentive and ability than its competitors to deter entry by creating a reputation for aggressive response. Sainsbury’s suggested that, for example, the threshold applied to retailers without national market power could be a 50 percent market share within the isochrone, but that this should be reduced to 40 percent for a retailer with national market power”.

I got it slightly wrong when I said 50 and 40. This is rejected by the Commission.

While it is true, of course, that more Tesco stores are affected by the test than stores of any one other retailer - because Tesco has more stores overall - the effect of the test on the other large retailers is also very significant, especially relative to the size of their businesses. Tesco refers at the outset of its notice of application to Table 6.1 in the report, to show the impact which the test has upon Tesco. But, it also shows impact on everybody else. That is Table 6.1 in Chapter 6, p.110. This is the ten minute isochrone table, and it is the ten minute isochrone which is used. You will see the number of stores in the left-hand column which totals the 495. I draw attention to the next column which is what proportion of that retailer’s largest stores -- what proportion of its business is going to be affected. You see it is 31 percent for Tesco, but it is 29 percent of all Morrison’s larger stores.

(After a pause): I thought it was agreed that this is not confidential in the end because it had been disclosed in an appendix. There was some correspondence about that.

THE PRESIDENT: The figures you are speaking about are in the non-confidential version, are they not?

MR. ROTH: Yes, that is my understanding. Somebody said ‘Confidential’. (After a pause): Withdrawn. I think that applies to all Mr. Green’s submissions.

MR. GREEN: Not quite!

MR. ROTH: 29 percent Morrisons. Waitrose - 27 percent of all their stores are affected. So, it has a very significant impact on the business of other retailers. Indeed, the Co-Op’s large stores are the greatest proportion of all. That is in terms of existing store expansion

obviously. You cannot tell about a hypothetical new store that it might have wanted to open. You would have to know where it is and draw the isochrone around it, and then see whether it is in a highly concentrated market, or not.

You will have seen from Chapter 11 of the report how, notwithstanding that, all the major retailers other than Tesco supported the concept of a competition test being introduced as part of the planning process, although they expressed different views as regards the detail or scope of the test. That is at para. 11.18. You will see that in Footnote 306.

So, I come to the irrationality argument regarding the test, which now seems to be the first ground of challenge by way of judicial review. I say that because you will have seen from the notice of application and our defence that there was an *ultra vires* ground which was alleged in the notice of application. We addressed that in our defence. It is not mentioned at all in Tesco's skeleton, or, indeed, oral submissions. We answered it in writing. But, it is said now, "It is irrational to introduce this test in the *Wednesbury* sense - that the Commission failed to have regard to relevant considerations, being the unmet demand or the costs resulting from the competition test".

> Mr. Green characterised the Commission's approach as finding unmet demand will be met by new entry or, as he put it, the virtuous circle of the market when he said, "Well, actually the findings in the report, when you look at them, contradict that view". But, with respect, that is a distortion of the Commission's whole approach in this sense: the Commission did not find that an adverse effect on competition was the persistence of "unmet demand" - customers not getting any supermarket, or not getting a supermarket that is sufficiently close to them. Since that was not the adverse effect on competition, the Commission found, that was not what it was seeking to remedy. "Unmet demand" exists all over the country in high concentration markets and in low concentration markets. There was reference to the LPA view of planning need as a proxy for that, whether it is an exact proxy or not. It does not mean, of course, that consumers have no grocery store. It means there is scope for more large grocery stores, or different large grocery stores that would give a consumer a choice of another facia. That is why, because of this unmet demand, that this is a dynamic market with all the supermarket retailers expanding.

The Commission's concern was something else. It was the persistence of highly concentrated markets which they found resulted in various identified customer detriments - the detriments that they summarise in paras. 10.13 to 10.15: deterioration of what is

referred to as the PQRS (price, quality, range, service) -- the retail offer in those highly concentrated local markets and a sort of indirect national effect on pricing because prices are set nationally for those supermarket retailers who have a high proportion of their stores in the concentrated market -- and the deterioration in choice.

So, the competition test does not address this "unmet demand" and, more specifically, if, in a highly concentrated market, the large incumbent has no desire or opportunity to open a new store or to expand its existing store, the competition test will not apply. There is nothing for it to bite on.

The Commission found that there was a barrier to entry and expansion from the general planning regime, including what is referred to as the "sequential test" which retailers objected to and made submissions about. So the Commission considered whether to recommend a change to the general planning system. They decided it was not appropriate to do that for reasons they give, and I will come back to that.

Subject to one qualification about the effect of expansion, the obstacle to growth from the planning regime applies indiscriminately to all grocery retailers. It is not targeted at any particular one. So it may mean that in a local market there is no growth in large grocery retailing floor space. But if, in a particular local circumstance, the incumbent – pausing there, I use the word "incumbent" to mean, as I think you all understand, not a monopoly market, but there is one large retailer with less than three other fascia and more than 60 per cent of grocery floor space, but that is rather a mouthful, so I will say the "incumbent" – if in the local circumstances the incumbent can surmount the planning obstacles, that barrier, and get planning permission for a development, then there is no basis for inferring that none of the other retailers could get planning permission for a development and that none of the others would be interested in development in that area.

What the competition test is doing is to achieve a situation in an area where expansion of grocery sales area is envisaged by retailers, in the light of the barrier to entry from the planning permission regime but nonetheless it could be overcome, then that development should not be undertaken by the one retailer that is in such a strong position in that local area that effect of that retailer carrying out the expansion or opening an additional stores would, on the Commission's factual findings, lead to a deterioration in the retail offering for consumers. In that way it is changing the competitive environment in those local markets. All retailers of course will take this into account, the effect of the test, in their strategic planning. These are all large companies, highly sophisticated national companies.

Moreover, if the situation in that local market is such that it is commercially rational for incumbent to seek to open a new store or expand an existing store, then if there are three or more other fascia in that local market, even though it is an over 60 per cent share, it is free to do so because the Commission considers there is sufficient choice. If there are no more than two other fascia then the test applies to that incumbent and such development is prevented. An incumbent, of course, knows that it will be prevented and its rivals know that it would be prevented.

That really takes one to the question which now seems to lie at the heart of Mr. Green's rationality argument, which is that where developments by an incumbent which would otherwise have taken place are blocked through the competition test, is there a significant or serious risk that, first of all, no other retailer in that market will seek to expand or open a new store – I will come to the monopoly market where there is no retailer in just a moment – but if there are others in the market, the other two fascia, neither of them would do it and none of the large retailers which are not presently in that market would seek to enter. I say this now seems to be at the heart of Tesco's case because you will recall that in the skeleton there were put a series of hypothetical examples and where it was said the competition test would lead to perverse results or damaged consumer interests. They were put in different ways and we answered each one of those in the appendices to our skeleton, and we have shown they are fanciful or wrong and none were now referred to. So I think it comes down to this case.

In the answer to that hypothesis or posited case, the Commission does indeed rely on the fact that this is a dynamic market with strong competition between large and sophisticated retailers which have been expanding and each looking for commercial opportunities.

Mr. Green said, "Oh, no, that is the UK as a whole, the dramatic and continuing rate of expansion in sales are, I think it is 38 per cent over seven years, that is across the United Kingdom, whereas here we are talking about highly concentrated markets". He now places repeated reliance in that regard on appendix 7.1, as you will remember, an appendix which one notes is not relied on in this context in either notice of application or the skeleton, but it is now very strongly in their case.

I will come in a moment to appendix 7.1, but before doing so one asks, is there any basis for thinking that the characteristics of rivalry between large supermarkets that is observed nationally on the figures, for growth, and so on, would be different in highly concentrated markets. One can say this: in its many and extensive submissions to the Competition Commission in the course of the enquiry, and I think most of them are in the bundles and

Mr. Freeman in his witness statement sets out the chronology, all the submissions that Tesco made in the meetings it had, Tesco never suggested that either they or their competitors are less keen to enter highly concentrated markets – that is say whether one of their competitors is the incumbent – than other local markets where the rivalry is already intense between the supermarkets. It would be very strange indeed if a supermarket was less keen to enter a highly concentrated market.

So one comes to appendix 7.1, and what it shows, if you could please turn that up. This is the famous persistence analysis. It was an analysis that was carried out, as the first paragraph explains, to assess:

> "… the extent to which those local markets identified by the CC as being high concentrated in its 2000 groceries market investigation continue to remain highly concentrated in 2006. The persistence of these concentrated local markets informs our analysis of barriers to entry in local markets."

In other words, it is an analysis carried out to ascertain whether there are barriers to entry on the existing scenario at all, and for that it used the information on monopoly markets and duopoly markets. It found that, in general, there was little change since the 2000 report. That led to the conclusion that there are indeed barriers to entry in those markets. The finding which appendix 7.1 really is the support for, and indeed the table is reproduced, is in fact in the main body of the report at paras.7.10 to 7.11. Can I ask you, please, to go there. 7.10 says:

> "We examined the experience of new entry near stores that faced few local competitors to assess whether highly-concentrated local markets have persisted over time. In 2000, there were 186 stores larger than 600 sq metres in Great Britain belonging to [the then big five] which faced no or only competitor in the local market in which they operated (monopoly or duopoly stores). In 2006, 160 of these stores (or 86 per cent) continued to face no or only one competitor (see Table 7.1). The persistence of local concentration is indicative of the presence of barriers to entry in the markets in which these stores are located."

There is the table which also appears in the appendix.

Thus the finding in appendix 7.1 that is incorporated here in paras.7.10 and 7.11 is part of the material that points to the conclusion that in the current situation there are barriers to entry. Then the Competition Commission in the balance of Chapter 7 proceeds to examine what the barriers are. One is the planning regime, another is control landsites. In general, and I say in general, because I will come to the exceptions, the Commission concluded that

the remedy of freeing-up controlled landsites and curbing expansion by the incumbent should encourage expansion by the other, if it is a duopoly market where, by definition, there is another one, or new entry by another retailer, even if at present it is a monopoly market, because the Commission did pay particular attention to the position in monopoly markets. They had that problem very much in mind because it was suggested to them that there are markets that might actually only be able to support one retailer or one large store – a natural monopoly. It was a point put by Tesco and I think also by Sainsbury's, and so they considered is it appropriate to cover natural monopolies in the competition test? Should there be an exception for that? They found that you cannot conclude that low population necessarily means that there is only scope for one store, and if there is more than one fascia well then the competition test would allow rivals to expand, and that is in 11.30, the monopoly market argument.

> "11.30 We explored the point, raised by Tesco and Sainsbury's, of whether there were 'natural monopoly' areas, in which the application of a competition test may be inappropriate. We note that some areas with low population, which might be expected to be 'natural monopolies', have more than one store."

And they give on example in the footnote, an extreme case, Huntly – 5000 in the town, 16,000 within a 20 minute drive time, therefore outside the isochrone, and others in appendix 7.1.

"However, we accept there may be areas where there are three or fewer fascias present and where the local population is too low to support entry by an additional fascia. It is important to note that our competition test would not have the effect of prohibiting all development by existing grocery retailers in the local area: rather it would prevent development that would lead to one grocery retailer having an unacceptably strong local market position, or strengthening of such a position."

So they consider that and address it, and then they go on to the point that was put by Tesco on this:

> "11.31 We assessed Tesco's claim that, on the basis of its reproduction of the first-stage regression of our margin concentration analysis, our analysis predicts that an increase of 34,052 people leads to an increase of one extra store of above 280 sq. metres. From this it told us that 34,000 more people within 10 minutes were required to support an additional store above 280 sq. metres – so only expansions and replacement stores would be possible."

The Commission considers that and comes to its view:

"11.32 We agree that there is a general positive relationship between population and the number of stores in an area. The first-stage regression results of our margin concentration also clearly show this positive relationship. However, the purpose of this regression is not to identify the exact relationship between the size of the population and the number of competitors and we do not think that these results show that 34,000 more people are required to support an additional store above 280 sq. metres."

So they consider the argument expressly, they come to their view and it is not said on the basis of that, that that is not a view they are entitled in assessing the evidence to come to. Indeed, what Mr. Green said to you yesterday that maybe Tesco put it too high, "let us say 8000" he said going through the appendix. This new hypothesis which, of course, was not addressed at this point in the Report, because at that point Tesco were saying 34,000, now they are saying "maybe it is 8000". It is also not self-evident, because it rests on the premise that the only customers that a new entrant would seek to attract would be the 8000 growth of population; you need a population growth of 8000 for anyone to come in. If there are less than 8000 another retailer would not come in because that number is too low to support the commercial operation viably of a new store. But, of course, a new entrant to a market is not just seeking to serve the population increase, it is seeking to compete head to head with the incumbent, and take market share from them. So population increase may create a new opportunity but it does not circumscribe the size of a new entrant store.

It was suggested by Mr. Green today, I think in answer to an observation from Professor Pickering, that this notion that the competition test facilitates, or encourages new entry, it was never made clear that that was the rationale of the test. He even said there was some failure to consult – he referred to *Interbrew*. With respect, that really is totally contrived. Tesco knew full well that that was the thinking underlying the proposal for the competition test. They acknowledged the point – they disagree with it, but they knew that that was what it was about.

Can I ask you to look at what Tesco said to the Commission in their response to the proposed remedy, which is in bundle 3.3, which is I think your bundle 5 at tab 54. This is Tesco's response to the provisional remedies' decision. It starts at p.2931 and if you go, please to p.2939, under the heading: "The CC's proposed remedy would distort rather than enhance competition" you see at 3.16:

> "The remedy presupposes that there is a shortage of sites and that if one retailer is prevented from developing a site another retailer will step in. Neither supposition is correct. We know, and the CC appears to accept, that sites for development are

> available, and we have explained previously some retailers' strategy, formats and/or demographic appeal prevent them expanding in certain areas. Similarly, others have been shown to have a less flexible, and in some case a more 'stop/start', approach to property acquisition.
>
> 3.17 Even in those areas where alternative entry would occur, barring investment by one retailer does not mean that customers will get a better outcome. Indeed, they may get a worse outcome if a retailer for whom there is less customer demand ends up entering the market. Since the Competition Commission has demonstrated no incumbency advantage (indeed, its analysis shows an incumbency disadvantage since self-cannibalisation is higher than rival store cannibalisation), the CC's approach will result in the promotion of less preferred competitors over the interests of consumers and the competitive process."

So Tesco is saying there "yes", your premise there, Commission, is that if one retailer is prevented it will encourage another to step in, we do not agree with that premise, but they are well aware that that is the premise. The suggestion that one had in the skeleton that all this is some new point developed by Mr. Freeman's witness statement, has come as a great surprise is just nonsense. Then they go on to say that even if new entry will occur that is not good because it effectively will not be Tesco's, it will be somebody else and not first choice. That was how they approached it at that point.

So, we say there would have been no basis for the Commission to find that in general there was a real concern that if one retailer was blocked by the competition test, no other retailer would step in. That is entirely contrary to the way in which the market was working. That approach is borne out by the submissions of the three large retailers who have intervened in this case. They know how competition takes place in these markets. Tesco seeks to dismiss, or sideline, the submissions of the interveners as being self-serving, being designed to further their own commercial interests. Well, members of the Tribunal, no doubt it is - as Asda, indeed, readily acknowledges and explains. But, coming from Tesco, the suggestion that you should dismiss or discount the submission of a large grocery retailer because it is motivated by commercial interests, well, that is, if I may say so, a rather bold - indeed, original - submission. Is the Tribunal really being asked to imagine that in bringing these expensive proceedings Tesco is not similarly motivated by commercial interest? Indeed, their skeleton, one notes, goes even further. In the core bundle you have the Tesco skeleton at Tab 4, sub-tab A. Right at the end, at the last page,

p.45, at para. 149, Tesco says about the interveners, in saying their statements are of little value,

> "They are not motivated by a desire to promote the public good".

Well, sir, if that is the approach that Tesco urges upon the Tribunal, I can truly say that there is only one party before you that is motivated by the desire to promote the public good -- indeed, mandated to promote the public good, and that is our client, the Competition Commission. It is quite wrong to say, as they go on to assert, "Well, the interveners are just offering bare assertions". Indeed, the Marks and Spencer statement of intervention includes specific material regarding its expansion plans that are so commercially confidential that they have been redacted. I have not seen them. I leave that point to be developed by their respective counsel.

Mr. Green made great play with one paragraph in our defence which shows that the Commission did not know whether new entry would occur. That is para. 102. You will remember that - we came back to it again and again. The defence is at Tab 2 of this bundle. It is discussing economic benefit, but he says that it applies here because the Commission is saying that it does not know whether new entry would occur. Mr. Green said, "Well, how can the Commission say", he asked rhetorically, "that it is self-evident that entry will occur when it has got not the faintest idea as to the benefit that the test might bring?" With respect, that is completely mis-conceived. Could you turn to the bottom of the previous page, p.33 of the defence? This discussion is under the heading 'Quantification of the Benefit'. It is referring to this, as you see from para 101,

> "The Commission made clear in its Provisional Decision on remedies that it had not, and could not, quantify the benefit arising in the future from the application of the competition test:
>
> *'It is clearly not possible for us to assess the scale of the detriment that would result from the emergence of local market concentration in the future. However, since our view is that local market concentration adversely affect[s] competition, we consider it likely that local market concentration that would emerge in the future absent our remedies would generate a significant consumer detriment'*".

In other words, this is dealing with a preventative aspect of the test - namely, areas that are not currently highly concentrated, but, in the absence of the competition test would become highly concentrated - the emergence in the future.

What para. 102, below, is saying is, "Well, regards that benefit, that is something the Commission could not calculate". Well, I will come back to that when I deal with benefits. Then he goes on in para. 103,

> "In contrast, data was available to the Commission on average revenue and costs figures and on the markets which are currently highly concentrated, enabling it to estimate the profits currently being urged by larger grocery stores in *existing* highly concentrated markets, which would not be earned in the presence of an additional competitor store within a ten-minute drive-time".

So, para. 102 is not dealing at all with the question of whether, where in a present highly concentrated market an incumbent is blocked from expansion, a new entrant is likely to come in. That is just not the point being addressed there. It is of no relevance to this.

So, I come, sir, to the LPA override, or safety valve.

PROFESSOR PICKERING: Mr. Roth, just before you move on - and I apologise because I am sure this is in the data - can we just clarify the basis on which facia are identified and intended to be identified? We obviously recognise that there are the facia of the major groups. But, could you just clarify how far down the list is the count of facia intended to go, and also what is the position regarding different facia in terms of reflection of different styles of retailing by the same group

MR. ROTH: On the second part of that question, I think this concerns only large grocery stores which are caught by the test. There is no suggestion in the report that within the same facia, once you are in the category of large grocery supermarkets, there are different styles within the same facia. One knows about the smaller stores - the convenience stores - that are operated by the same groups ----

PROFESSOR PICKERING: They would not be caught by the test.

MR. ROTH: I believe that is right (After a pause): No, they are not caught.

PROFESSOR PICKERING: Thank you for clarifying that.

MR. ROTH: It is only either a new store that is over 1,000 sq.metres or expansion of an existing store that is either already over 1,000 or the expansion will take it to be over 1,000.

PROFESSOR PICKERING: If I were running one of these major groups and was constrained by the 60 percent and the other facia counts and decided to introduce another facia, a variant, would I still count as part of my original facia?

MR. ROTH: Yes, I understand the question. Can I just take instructions? (After a pause): I am told it would count as the same facia, even if it is given a different name.

PROFESSOR PICKERING: It is group ownership.

MR. ROTH: It is group ownership, yes, but only the large sites.

PROFESSOR PICKERING: Thank you. That is helpful.

MR. ROTH: Otherwise, of course, there would be a very easy way.

PROFESSOR PICKERING: Precisely.

THE PRESIDENT: I am sure you are going to deal with this, the rationale for the remedy and the benefit, as it were, but the distinction you draw in answering Mr. Green's point about para.102 is the preventive approach, the effect of the remedy on avoiding, preventing, further concentration of markets where they do not exist already and any effect that the remedy might have in relation to markets that are already concentrated.

MR. ROTH: Yes, and all 102 is saying is that that aspect, because this is answering a criticism, you could have quantified the benefit, which I will have to come back to, is something you cannot do for the potential future.

THE PRESIDENT: Forgive me now, the answer may be obvious, but is the remedy aimed at both situations?

MR. ROTH: Yes.

THE PRESIDENT: Competitive, and it is designed to cure the existing situation.

MR. ROTH: It is designed to prevent, which it will have with immediate effect, once it is eventually adopted, and it will have that effect in two respects. One is that it stops, which is what 102 is saying, a market that is not presently highly concentrated becoming highly concentrated. Secondly, it will stop a market that is probably highly concentrated becoming more concentrated, the market where it is over 60 per cent going to an 80 per cent share. Thirdly, it will facilitate new entry in markets that are highly concentrated.

THE PRESIDENT: It was that third point that Mr. Green, as I recall, claimed was not developed in the Report and could not easily be found. Can you point us to that?

MR. ROTH: What I was going to do, but I can change the order if you wish, was to come back to that under "Is it an effective remedy?" and deal first with the LPA. I will then come back to that, if that is acceptable. Thank you.

In saying that in general terms there is no basis for assuming that another supermarket will not come in because the competition test is, and is very deliberately, a mechanistic test. As the Commission states in several places in the Report it was seeking to set out a test that is clear, certain and easy to apply, because there are obvious benefits and efficiencies from that, including that it should become largely self-policing and then the retailers will know if they are caught or if anybody else is caught, whether their rival is caught and what that means for their opportunities.

Like any mechanistic test there will obviously be cases where a development that should be blocked on a thorough analysis of the local market and the particular local market conditions might pass the test and get through, as it were, and go ahead. Similarly, there will be cases where something will be blocked by the competition test and yet another retailer will not undertake the development. That is why the LPA override is important. Mr. Green stressed the fact that the Commission say, "This is to apply only in exceptional cases". Indeed they do, consistently with the rationale underlying the development of the test that in the generality of cases where a development is considered to bring benefits in terms of meeting demand. Another retailer would undertake that development, given the dynamic nature of the market and the companies one is dealing with. Since it is a single clear test applied right across the country and there will be local variations, so the Commission recognises that there are exceptions which the local planning authority is best placed to assess. That is what 11.53, where the override is set out in the reasons, says. They say it should be a truly exceptional case.

THE PRESIDENT: 11.54 shows it is intended to be quite a high hurdle, is it not?

MR. ROTH: Yes, absolutely.

THE PRESIDENT: Because they have got to prove a negative, they have got to make out a convincing case why another retailer would not be prepared to take on the project, and that may involve some market testing.

MR. ROTH: Absolutely, it is no good just coming along and saying, "We are willing to do this, nobody else is, so please can we have planning permission although the OFT has said or is about to say, or we know they are going to say, that we have over 60 per cent". That will not do. They have got to do more than that. If that would do there would be a very easy way to drive a coach and horses through the test. Equally, a planning authority is not just going to accept a statement from another retailer saying, "Oh, yes, we would do it", they will want some details of where and when, and so on, so they will have to test the situation and assess whether it is right.

The test was designed, the override, having regard to one of the objections that Tesco put in its submissions on the proposed competition test, as you can see at 11.19.

> "Tesco, on the other hand, was strongly opposed to a competition test. It did not think that we had identified an AEC that justified a competition test (which it referred to as a 'local growth cap'). Tesco also considered that a competition test would not address the feature of the market we had identified as giving rise to this AEC. Tesco said that a mechanistic competition test would:

- be anti-competitive and wrong in principle;
- lead to less investment and fewer stores in marginal areas where other retailers would not develop despite the existence of significant public policy benefits."

It is in recognition of that that there will be the marginal areas that the LPAs are given, but under, yes, strict conditions of how it can be applied, so that it cannot be used just to effectively water down the whole operation of the test that is designed to address the AEC, and that it is there.

Then also I think there is the third bullet from the end of that paragraph:

"Limit LPAs' ability to approve developments which would benefit customers and communities such as regeneration schemes."

There is another objection being put that it may be that the supermarket is part of a wider scheme that will bring inner city benefits, and if you block it those benefits will be prevented, and so the LPA is left with the potential for assessing that and then overriding the test and saying, "Yes, the OFT is satisfied this will increase concentration in a highly concentrated market, but nonetheless it can go ahead".

These retailers are all well used to dealing with local planning authorities. They have already got to work with the needs test – it may in future be abolished, but they have been working with it for a long time – and satisfy the authority that there is demand.

What one is envisaging is that an LPA which is dealing with a particular application in its locality, it gets the certificate from the OFT saying, "This is an area of high concentration", it has got the Competition Commission report saying what is the effect on the local store offering in areas of high concentration, and they will have to test and make sure that no other retailer would undertook a similar development. Also it has to publish its reasoning. I think it is hardly a criticism that the LPA has to publish its reasoning rather than keeping it secret. All this takes place as part of the planning process. Yes, the Competition Commission thought this is very much an exceptional case. That is because the Competition Commission thought that in the great majority of cases another retailer will undertake a development. It is entirely consistent with the whole way it approached it, but there is that safety valve put in.

Then one asks, taking it all together, is this an effective remedy to the AEC and the customer detriment which the Commission has identified? That, I think, goes with Mr. Green's over time point and goes with also Mr. Mather's question: "How far is that the effect of the remedy indicated in the Report?" because that was all conceded. What the Competition Commission had to do, having identified the adverse effect on competition,

having found the customer detriments that result from that AEC, then to say what are the possible remedies that one should consider to deal with that? How would they work? One remedy that it considered was the remedy of divestment, because that is a fairly simple remedy in one sense. You have a highly concentrated market, in those highly concentrated markets where you have multiple stores in single ownership – it obviously does not help where you have not – but in those, and I think there were over 50 of them where that is the situation, a direct and rapid means to reduce concentration is divestiture. So they considered: is that the approach that should be taken? That is 11.263 under the heading: "Multiple trading stores":

"11.263 The most direct means by which we could address the 57 stores in highly-concentrated local markets where one (or more) grocery retailer owns or controls more than one trading grocery store is by requiring the occupancy of (at least) one of the multiple stores by another retailer which would increase the degree of competition in the local market."

The next paragraph considers leasing and they say that is ineffective. 11.265:

> "We explored the question of whether compulsory divestiture of one or more of its stores in a market by the strongest grocery retailer in that market would be an appropriate remedy. We considered the costs that the retailers would incur as a result of any such divestitures. In most of these cases we would expect vigorous competition from other grocery retailers to acquire any divested stores and would expect the vendor to achieve the full market price. The purchase price may be less than the store was worth to the vendor, as it would not include any premium for expected monopoly rents, but this is precisely the problem we would wish to address and it is not something we consider we should take into account. However, we recognise that divestiture represents a very significant intervention in property rights."
>
> 11.266 We also believe that there is a significant difference between store divestitures and the other remedies we decided to pursue in relation to highly-concentrated local markets. Whilst our other remedies will ensure that grocery retailers have the opportunity to enter a market to establish a new competing grocery store in the future …"

i.e. facilitate entry –

> "… store divestitures involve the transfer of ownership of an existing trading store. In our view such a transfer could have a disruptive effect on consumers in

the short term. Those customers who have chosen to shop at the divested store and who are familiar with that store will either find their store operated by another retailer or will have to find an alternative store to continue shopping with the same retailer."

11.627 In Section 6 we identified two effects resulting from highly-concentrated markets. The first effect relates to a lower standard of retail offer in the local markets themselves, and the second relates to the weakening of those components of the retail offer, such as price, that retailers choose to apply uniformly across all the local markets in which they are present.. We believe that the second of these effects will be effectively addressed by the package of remedies we decided to pursue in respect of existing and future controlled landsites (together with the inclusion of the competition test in the planning regime and the requirement on large grocery retailers to notify acquisitions of existing stores in excess of 1,000 sq. metres). We decided that the gravity and prevalence of our AEC finding in relation to these markets in respect of the first effect is not sufficient to justify a divestiture remedy.

11.268 Divestitures would represent a significant intervention in property rights, as well as being disruptive to consumers. We do not believe such an intervention is supported by the gravity and prevalence of the AEC we found. Moreover, we note that store development is a continuing feature in grocery retailing, with the four largest grocery retailers having expanded their UK sales area by 38 per cent between 2000 and 2007. Given t his, it is our view that removing barriers to entry in highly-concentrated local markets …"

Pausing there, that is the controlled land remedy, of course.

"… and ensuring that store developments do not exacerbate high concentration will be sufficient to address the AEC we have found in relation to highly-concentrated markets so that there is no need for us to require store divestitures. Indeed, store divestitures in these highly-concentrated local markets would not effectively address concentration: they would constitute a very limited and one-off intervention in a large and dynamic sector. We therefore believe that the competition test and the controlled land remedies will be more effective remedies over time than would be store divestitures."

So they are saying in other words that store divestiture is too draconian, although the benefits are immediate and could be more easily calculated, and they would not have any

effect on preventing areas of high concentration arising, whereas the controlled land remedy and the competition test over time will be sufficient to address the AEC "we have found in relation to highly-concentrated markets". How does that happen? because there is new entry into those markets, and the concentration goes down. The controlled land remedy, of course is not only addressing existing controlled land, it also prevents further controls and restrictions being imposed.

THE PRESIDENT: Leaving aside the preventative part of it, in that para. 11.268, it does two things. It ensures that the store developers do not exacerbate the high concentration and that is sufficient over time to address the AEC. Now, "address the AEC", I think the point that is made against you is that first of all "over time" can mean anything, it could be 100 years; "address the AEC" does not tell you anything about how much of the AEC is going to be addressed. Is it going to remove the majority of concentrations over time, or all of them, or a significant percentage of them? That is the sort of pointer that, speaking for myself, I would appreciate assistance on eventually

MR. ROTH: Yes, indeed, Sir. I think those go to the question of quantifying the benefit, namely to what extent over time ----

THE PRESIDENT: And I know you are not particularly on that at the moment.

MR. ROTH: And that came over proportionality so I have not come to that, but absolutely I am fully conscious ----

THE PRESIDENT: We are still on ground one, are we?

MR. ROTH: We are still on ground one, but I need to deal with those points. What I am dealing with is, is it envisaging that they will be facilitating new entry? Is that indeed part of the reasoning? I am saying "yes, it clearly is."

Similarly – and perhaps I should have taken this first, because it is a bit earlier – one of the first things the Commission considered is: should we recommend a reform of the planning system generally. One remedy I think all the retailers were saying "Yes, please. Can you make it easier to enter markets." So they looked at that and took into account the fact that there is this proposed reform of the planning laws under discussion, I think the Barker Report and a White Paper that resulted, and they also asked: "In the light of that is it really necessary to have this competition test?" and they said "Yes, it is" and one sees why. This is at 11.24, which refers to the current planning and the needs test and says, in the second sentence,

> "This means an LPA currently does not have the ability to consider the consequence of 'need' being met by a particular operator, according to how that particular operator may create or strengthen an area where it has a strong local market position. We discuss the 'need test' more specifically in our discussion and proposal to modify the planning system
>
> The town centre first policy may help to promote competition insofar as it results in grocery retailers being located in close proximity to each other. However, we note that the identity of the operator, which is a key criterion in assessing the extent of competition is not taken into account in PPS6, in the town centre first policy. Nor is this proposed for England"

Then there are some details of that.

"We do not consider that such a focus would evolve without our intervention. Even with the town centre first policy in place, for large grocery retailers with large grocery stores we have identified 495 highly concentrated local markets within a ten-minute drive time and 209 stores within a fifteen-minute drive-tie. We do not think we can rely on this policy alone (despite the consultation paper on PPS4 and the likely amendments to PPS6) to prevent the emergence of such areas in the future, or to encourage development which would increase competition in existing highly concentrated local markets. In order to achieve this, it is our view that a specific focus on the identity of the operator is essential". I am quite clear that is what they are trying to achieve, and that is why they say, "No, the planning development will not do that for us".

I should say perhaps that both 11.25 and the one I read before which refers to 'over time', 11.268 -- Neither of those are reasoning in the report that Tesco is seeking this Tribunal to annul. They are not the identified paragraphs in the letter from Freshfields asking what particular remedy they are seeking.

Now, the question of 'over time' I will come back to when I deal with benefits. However, let me say this about it now: We say that the time in which remedy will take effect is a classic example of a matter of judgment for the Competition Commission to decide. They do not have to specify a time in which the remedy will apply. Of course, their guidance says that in general they prefer remedies that work in a shorter time than a longer time. That is obvious. But, they tailor the remedy to the situation and the nature of the market - a point, I think, made, if I may respectfully say so, very pertinently by Professor Pickering. There is no doubt that divestiture for those fifty-seven markets would work very much quicker in a short-term sense. That does not mean they have got to go for divestiture. They

can say, “No - they are competing considerations”. I am sure that if they had gone for divestiture, that would have been something else that would have been challenged because it is far more intrusive ----

THE PRESIDENT: I think the point is more subtle than that, is it not, Mr. Roth, because what is said is, “Well, if you are not going for something where you can get a handle on the timing, such as that, divestment would be self-evidently immediate”. But, where you adopt a different remedy - such as the competition test - if you are going to judge the effectiveness of that remedy to achieve what you wish to achieve, you must have, must you not, some idea of how, how much, and how soon? Are those not relevant to effectiveness?

MR. ROTH: You have to have a sense that it is going to be within a reasonable time, yes. But, I do not think you have to resist any suggestion. With respect, you have to say, “This will, in seven years, mean that of the 495 areas, 313 will have become less highly concentrated, or even two-thirds of them”. You can say, “This will change the market dynamic and in the competition that exists between supermarkets, and with the process of expansion going on, it will lead to the matter being eroded year by year. Things will improve year by year”. They consider, in their judgment, as the expert body - at 11.268 - that this will be sufficient over time to address the AEC that they have identified. So, it may not be required to say that it will do it in five years, or three years, or ----

THE PRESIDENT: Not even a ball park?

MR. ROTH: It is clearly within a reasonable time, but they do not have to set out what that will be in the way that this market is working.

PROFESSOR PICKERING: Part of competition policy guidance does tend to distinguish between responses in the market that would occur within two years and those responses that will be likely to occur but beyond two years. Different views as to the welfare benefits of the alternatives are expressed. So, is there ground for concern that perhaps the Commission has not attempted to say at least how quickly it thinks that there would be some material gain?

MR. ROTH: I think what it is saying is that there will be material gain year by year, but that AEC breaks down into different aspects. There is the AEC from the existing areas of high concentration. Well, that is something that will be addressed year by year as a gradual process. There is the AEC that would arise through the creation of new areas of high concentration that are not presently – well, that is addressed preventatively immediately. Different parts of the remedies come into play. The remedy on exclusivity agreements on land sites is to put a cap on five years - so that after five years on those developments you

can have another retailer coming in. So, in five years' time there will be an opening up of further opportunities. Yes, it is in a foreseeable timeframe, but it is certainly not seeking to say that within two years these 495 areas of high concentration will not be areas of high concentration. In no sense is it saying that. So, one is looking at a reasonable timeframe of five/ten years. One is looking ahead.

THE PRESIDENT: It does not say that though, does it? You are saying that, but it does not actually say that anywhere.

MR. ROTH: No - because it may be 12. I am not saying that at the end of ten years ----

THE PRESIDENT: It may be one hundred. The point is that it does not actually say what it means in terms of a timeframe. You are right, of course - prevention will occur straightaway presumably.

MR. ROTH: Yes. What they conclude is that this will be sufficient over time to address the AEC. If the criticism is that it takes too long, then one is left with there being divestiture as well - which is what they consider to have a more immediate effect.

THE PRESIDENT: But, by 'address' you interpret that as meaning that they will deal with it all - ultimately, all the existing concentration areas which are causing concern will have become de-concentrated.

MR. ROTH: No, not all of them because -----

THE PRESIDENT: Apart from the exceptional matters.

MR. ROTH: Yes, apart from the exceptional matters.

PROFESSOR PICKERING: What we are perhaps saying are two things: that it would address the AEC prospectively in a timeframe relative to the timeframe that the planning regime necessarily involves. So, entry is going to be slower than in some other businesses because there are other hurdles to go through. Perhaps also - and we have not actually used this term in this case so far - the mechanism is essentially the mechanism of the invisible hand, is it not? It is the profit motive of individual operators that will drive the facilitation, or will benefit from the facilitation that the test is intended to offer. Is that a fair comment?

MR. ROTH: Absolutely. Absolutely, sir, yes. It would not be something the Commission could do, other than divestiture -- sort of mandate new entry. Clearly not. It can do so here because it knows that this is a market that has been growing -- where you have a number of large sophisticated entrepreneurial supermarkets that have all been growing around the country and that are looking for opportunities to grow. So, the invisible hand in this market, unlike certain other markets where we know the invisible hand has rather let us down recently is working.

Mr. Green said, I think this morning, you can only rely on a remedy operating over time through the working of the market when there is no barrier to entry. With respect, that is completely upside down. If there was no barrier to entry there would be no need for this remedy at all. It is because there is the barrier to entry that you need the remedy. Given that, for other reasons, the Commission has considered it should not be recommending a change in the planning regime because that serves wider purposes and social objectives, therefore it restricts its remedy to the control landsites and to this limited remedy of the competition test.

We say that one cannot draw an inference from appendix 7.1, the famous persistency analysis, as to the time in which remedies will have an effect. Mr. Green said, look at that if nothing is going to change – because that is what is looking at what happened in highly concentrated markets without the remedies. Indeed it represents a part of exactly the situation that the remedies are being introduced to address. I think Professor Pickering, if I may say so, gave the answer to that point to Mr. Green. That is historic under the old framework. It does not tell you anything about how things would operate once you have a competition test in place and once you have the controlled landsite remedy. So it is not a predictor for what is a very changed environment, quite aside from the fact that, of course, 7.1 is only dealing with the monopoly and duopoly markets and not markets with three fascia or four fascia.

Mr. Green also referred in this context to para.52 of our skeleton, and that is in your bundle 22, our core bundle, at tab 4B. This was written in response to a submission by Tesco that the competition test would cause delay in development. All that is being said in para.52 is that there is no reason why, with a competition test, new store development should not occur as quickly as under the existing arrangements. The clarity of the test means that the grocery retailers can be expected to take into account to take it into account when planning their schedule of developments. Developments that would fail the test in a particular location will in all likelihood not be submitted to the planning process, while grocery retailers who are not restricted by the competition test will be free to undertake developments in that location, and such developments need not even take the form of new sites. Demand may be met by expansions or reconfiguration of existing stores. To suggest that retailers will conceive the possibility of expansion or new entry only after an incumbent retailer's development has been blocked is implausible naïve. In other words, we are meeting his argument that this is going to cause a lot of delay because you have to have one retailer who puts in an application and gets blocked by the competition test and

then another retailer, seeing that that application has been blocked, then says, "Ah, great", and develops its plans for development in that location. We say that is not realistically how things are going to happen. It has nothing to do with the issue of the over time point, it is dealing with a quite different point.

I am sorry, I have slightly jumped out of order, but I am going to deal with the question of the suggestion that there should be general remedies to the planning regime. I dealt with the consideration by the Commission of whether the government's anticipated proposals meant that a competition test was not necessary and why they said no. There was also the proposal from the retailers as to why they did not change the planning regime generally. That is at paras.11.133 to 11.135. 11.135 says:

> "We recommend that LPAs take greater account of competition in their development plans. We decided not to recommend any specific changes to the planning system (beyond the competition test). We are concerned that there is a risk of unintended consequences that could arise from interfering more than is necessary with an area of policy that has specific and well-defined social objectives and which is itself subject to a process of public consultation and reform. It is important to note that in choosing and designing our remedies in relation to the planning regime, we have taken account of the reforms proposed in the Planning White Paper. Our remedies are additional to those reforms and do not preclude any of the reforms proposed in the Planning White Paper in any way."

That is also something that the Commission took into account.

So we say that within that margin of appreciation in considering, is this as comprehensive a remedy as is reasonable and practicable, that is something that the Commission was well entitled to decide and conclude. It cannot be said to be irrational. It took into account the situation of suggested monopoly markets, it took into account the question of minimum economic size, it taken into account prospects for entry.

So I come to proportionality. I want to deal with that under four heads: first, to ask what is the relevant legal principle; secondly, does that principle oblige the Commission to carry out an impact assessment or cost benefit analysis, or whatever one wants to call it, of the competition test; thirdly, was the relevant principle correctly applied here; and fourth, in any event, could the benefit of the competition test have been quantified in a meaningful way on the information the Commission has. That is the schedule that Mr. Green handed up this morning.

I start with the relevant legal principle, and I do that because we say that it is very important to appreciate at the outset how proportionality comes to be engaged in this case, because that affects the substance. That affects the way the proportionality applies, and the degree of scrutiny that it involves. In the notice of application Tesco put this in terms of human rights. It is in your core bundle 22, tab 1 – p.14, para.20:

"Planning rules are prima facie interferences with rights of property protected by the European Convention on Human Rights *Pine Valley Developments Ltd. V Ireland* (1991) 14 EHRR 319. Any Commission recommendation to alter planning permission must therefore be proportionate. It must be (i) rationally connected to the objective which it seeks to achieve; (ii) limited to what is necessary for the attainment of that objective; and (iii) attended by no disadvantages other than those which are acceptable having regard to the value of the objective. The review court is bound to scrutinise the recommendation carefully to ensure that it is."

We dispute that this is anything to do with human rights, or that that sort of scrutiny applies. *Pine Valley* was indeed a planning case, but in the present case the competition test no human rights or fundamental rights of Tesco are engaged by contrast with the situation in *Pine Valley* and if I could ask the Tribunal to please be given a copy of that judgment.

(Document handed to the Tribunal)

This is a judgment of the European Court of Human Rights, following an opinion from the Commission. A case against Ireland concerning land development, just picking up the beginning of the headnote on the cover page:

> "The first applicant [Pine Valley] purchased a plot of land in 1978, relying on an existing grant of outline planning permission for industrial development. Detailed planning permission was originally refused by the planning authorities on the ground the property was part of a planned green belt. In May 1981 this decision was overturned by the courts on appeal by the first applicant. In July 1981, the first applicant [Pine Valley] sold the property to the second applicant …"

That is, I think, Healey Developments –

> "… which was owned by the third applicant [Mr. Healey]. The original grant of outline planning permission was held by the Irish Supreme Court in February 1982 to have been *ultra vires* and nullity *ab initio* since it was contrary to the relevant legislation. The applicants also believed the refusal of planning permission was not reversed by the Local Government (Planning and Development) Act 1982 which validated grants of planning permission

irrespective of the earlier legislation. Their belief was confirmed by an *obiter dictum* from the Supreme court. The applicants claim the Supreme Court's decision and the non-application of the 1982 Act violated Article 1 of Protocol No.1 to the Convention …"

and various other violations were also alleged.

If one goes to p.333 in the Report, just for convenience because it sets out the text of Article 1 of Protocol 1, the property right, at para. 49 – a familiar provision but just to remind oneself:

"Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."

That is the Article. Then in the judgment, going right on to p.354:

"*II Alleged violation of Article 1 of Protocol No. 1.*"

The applicants submitted that, as a result of the Supreme Court's decision holding the outline planning permission to be invalid, coupled with the respondent State's alleged failure to validate that permission retrospectively, or its failure to provide compensation for the reduction in value of their property, they had been victims of a breach of Article 1 …"

I am sorry, it is set out here as well.

"A. *Whether there was an interference with the right of the applicants*", and the court sets out the first question: whether they ever enjoyed a right to develop the land? They said that they did and the fact that it was void *ab initio* does not change that.

Then over the page, para.53:

"The applicants accepted the Commission's view there had been no interference with the rights of Pine Valley since it had sold the land in question before the Supreme Court's decision in the first Pine Valley case with the result that losses were borne by the other applicants.

Whilst the existence of a violation is conceivable even in the absence of detriment, the Court concurs in the result. Pine Valley had parted with ownership

of the land without retaining any right there over that was protected by Article 1 of Protocol No. 1. That provision, whether taken alone or in conjunction with Article 14 of the Convention, therefore did not apply to this applicant."

So that is the first applicant, Pine Valley. Then para. 54:

"The Court thus concludes there was an interference with the right of Healey Holdings (the second applicant) and Mr. Healey (the third applicant) to the peaceful enjoyment of their possessions.

This conclusion not affected by three other points on which the Government relied."

Then:

"55. The applicants contended that the interference in question, by annulling the outline planning permission, constituted a 'deprivation' of possessions, within the meaning of the second sentence of the first paragraph of Article 1 of Protocol No. 1. The Commission, on the other hand, saw it as a 'control of the use of property' within the meaning of the second paragraph of that provision.

56. There was no formal expropriation of the property in question, neither, in the Court's view, can it be said there was a *de facto* deprivation. The impugned measure was basically designed to ensure the land was used in conformity with the relevant planning laws and the title remained vested in Healey Holdings, whose powers to take decisions concerning the property are unaffected. Again, the land was not left without any meaningful alternative use, for it could have been farmed or leased. Finally, although the value of the site was substantially reduced, it was not rendered worthless, as evidenced by the fact it was subsequently sold in the open market.

Accordingly as, for example, in *Fredin v Sweden* the interference must be considered as a control of the use of property falling within the scope of the second paragraph in Article 1."

and then they go on to say that conformity with planning legislation and there was no violation of the second paragraph of Article 1."

So that was a case where what happened was land had planning permission and was purchased by Healey Holdings and Mr. Healey, with planning permission and then subsequently after they got it with planning permission there was then that judgment that set the planning permission aside, and so they lost value in the land which they had, namely, because the land had the planning permission and therefore there was an

interference within the second paragraph of Article 1, albeit there was then held to be no violation because it was under … pursuant to planning legislation.

Here, the competition test does not even get past the first hurdle, there is no interference. This is not encroaching on any existing grant of planning permission; it is an additional provision for planning applications for the future, and no property owner has either a fundamental right to be granted planning permission or indeed a legitimate expectation that the basis for the planning regime may not be changed for the future.

The importance of all this is that the present case, unlike *Pine Valley*, is not concerned with proportionality in the context of an interference with fundamental rights when, on the authorities, a strict proportionality test applies. It applies because you have to justify an interference with a fundamental right, and that is a rather strong thing to do. It might have been different, I can see, if divestiture had been the remedy. There you would have an interference and you would get into Article 1 territory. However, one notes in *Somerfield*, where that argument was put, it was held that, "Yes, you are within Article 1, but it is justified, and so no interference".

But, in the present case, this is not a fundamental rights case at all. We take strong issue with para. 20 of the notice of application. Here, proportionality is directed at simply whether -- What it means is: Is there a fair balance between the competing considerations of the ends and means? The court will interfere with the decision-makers' balancing in that regard only if it is manifestly disproportionate. We refer in our skeleton argument at Tab 4(b) to the statement of principle from *De Smith* (para. 24, p.12).

> "Proportionality as applied in the law encapsulates the concept of a 'fair balance' between competing consideration of means and ends".

The quotation,

> "Courts will not normally interfere with the balance of relevant considerations or with the impact of the decision unless it is *manifestly* disproportionate, so here too the burden of argument rests with the claimant".

We note in the footnote that if there is interference with a fundamental or human right, then the burden is on the public authority to justify what it is doing, and there is a more intrusive approach.

We refer also in the next paragraph to community law where it has been developed. This is the *ex parte Fedesa* case. The quotation is from para. 13. It is perhaps convenient to take them here.

"By virtue of that principle, the lawfulness of the prohibition of an economic activity is subject to the condition that the prohibitory measures are appropriate and necessary in order to achieve the objectives legitimately pursued by the legislation in question; when there is a choice between several appropriate measures recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued".

Again, that case, the ECJ, which concerns the Common Agricultural Policy, said the measure can be impugned on proportionality grounds only if it is 'manifestly disproportionate'.

THE PRESIDENT: That was because in those cases the Commission had such a key position in relation to all the complex agricultural ----

MR. ROTH: Indeed, yes.

THE PRESIDENT: It is interesting because everyone accepts that proportionality applies. I think Mr. Green said that it came in as part of reasonableness. You accept that it does apply. But, the quote from *De Smith* is very brief, and it does not provide much in the way of explanation as to precisely what kind of proportionality, or whether one ----

MR. ROTH: Yes. We all accept it applies, but then the question is: Well, what does it actually mean? Then one looks and asks: What actually does that test break down to? The point I am making is that actually it means different things in different contexts. One can bandy the word around - 'proportionality' - but it has been developed in a very structured way with a strict burden on an authority that is interfering with fundamental rights.

THE PRESIDENT: Sure. Yes.

MR. ROTH: Free movement in an EC context.

THE PRESIDENT: I suppose if something is disproportionate -- It may be that it is simply a relevant consideration whether something is proportionate or not. Is it effective?

MR. ROTH: Is it reasonable?

THE PRESIDENT: Although reasonableness has this connotation of irrationality which is slightly more ----

MR. ROTH: Yes. I was using 'reasonable' in the colloquial sense - not *Wednesbury* reasonableness, which is one that did not embrace proportionately.

THE PRESIDENT: As we have to apply judicial review principles here ----

MR. ROTH: But not the strict principles that have been developed for human rights cases.

THE PRESIDENT: I take your point on that. You say that it is not engaged -- the Convention is not engaged.

MR. ROTH: The Convention is not engaged. It is not a burden on us. It must not be manifestly disproportionate. There must be a reasonable relation between means and ends. We say that that is what it means in applying s.134(4), and that it is correctly reflected in the Competition Commission's guidance because the Commission has always accepted, yes, it must be proportionate. But, they put it in a rather different way from this. We say they put it correctly as to how it should apply. Look, if you would please, at that paragraph in the authorities' bundle at Tab 21. This is the guidance of June 2003. At p.40 is para. 4.10 - 'The cost of remedies and proportionality'.

> "The Commission must have regard to the reasonableness of any remedy and will aim to ensure that no remedy is disproportionate in relation to the adverse effect on competition and any adverse effects on customers [those being the criteria in s.134(4), you will recall] Part of its consideration will include an assessment of the costs of implementing a remedy, for example in disbanding or modifying a distribution system; and the costs of complying with the remedy, for example, providing the OFT with period information on prices or margins. However, the Commission must consider the wider picture. Adverse effects on competition are likely to result in a cost or disadvantage to the UK economy in general and customers in particular. Where significant, these costs might usually be expected to outweigh the costs incurred by any person on whom the remedies are imposed. If the Commission is choosing between two remedies which it considers would be equally effective, it will choose the remedy that imposes the least cost or that is least restricted".

We say that is the correct approach for the Commission to apply - assess the remedy, the costs of the remedy, as against the scale of the AEC that it is seeking to address. That is the approach that is set out in the guidance. As you appreciate of course, this is statutory guidance in the sense that it is published under s.171(3) of the Enterprise Act. I do not think there is any challenge to guidance as being wrong. The Commission can depart from its guidance, but it would need a good reason to do so. There is nothing in the guidance to suggest that proportionality requires the carrying-out of a cost benefit analysis or impact assessment, or similar, as regards evaluation of the remedy. I am not aware, in the numerous cases now of judicial review - countless cases of judicial review in the courts - dealing with proportionality in general terms that there has been held to be under the general law a requirement to carry out any sort of impact assessment by a decision-maker whose conduct is being impugned. Certainly Tesco has not cited any judicial review cases

generally. What they do rely on are two cases applying different statutory scheme where the terms of the statutes at issue required specifically this form of assessment of the measure that the regulator imposed. Then they rely on some Ofcom guidelines and they rely on the Green Book.

MR. MATHER: I think Mr. Green's point was slightly different, as I understood it, in that whilst the De Smith point and the authorities on judicial review accept the margin of appreciation, which essentially is what you are describing in the balance of relevant considerations and the impact of the decision -- I thought his point was, rather, that unless in current conditions some quantification was undertaken, it would not be possible to take such a decision properly -- there would not be the basis on which to choose in the first place.

MR. ROTH: Indeed, Sir, that was part of the submission he was putting. What we are saying is, yes, proportionality is an accepted principle, but it has never been applied to say that you have got to undertake some sort of quantification. It is not as rigorous a concept as that. Yes, the *E.On v. GEMA* case and the *Vodafone* case do impose that requirement, but for particular reasons under the particular statutory scheme.

MR. MATHER: Yes, I am sure that it is clear that there are different statutes applying which oblige those authorities to have a more formal impact assessment. It is equally possible to say that the general science of regulatory decision taking has advanced significantly in this area in recent years. These guidelines date from 2003 and in 2007 or 2008 a body properly carrying out its responsibilities would go through a much more formal quantification than in former years.

MR. ROTH: We say, with respect, that these guidelines of 2003 and the cases on judicial review have been flowing, indeed flooding, and since 2003, so that in 2006, 2007 and this year there have been many such cases on proportionality, and never has it been held that under the general law where you have not got a specific statutory requirement the public decision maker has to engage in some sort of quantitative analysis that goes beyond what 4.10 says, namely, look at the objective and the scale of the AEC and the look at the costs of the measure addressed to it and you do not have to do this complex detailed assessment of each particular element of the remedy. It is a point that would go, and I will come back to it, not just of course to the competition test, it would go to the other remedies. It would have to be evaluated applying that sort of quantitative, qualitative mixed *calculus*.

PROFESSOR PICKERING: Paragraph 4.10 talks about costs, the costs that arise from the AEC, and those are to be set against the costs of implementation and compliance. If the AEC is not fully addressed then the benefits from the remedy are likely to be less than the costs

from the AEC originally and there is no suggestion that the costs of implementation and compliance should be assessed against the actual expected benefits rather than the overall costs of the AEC.

MR. ROTH: I think there is no such suggestion in 4.10, and one can see that if a remedy was only dealing with one little aspect of an AEC one would say that then would not be a reasonable approach. Where a remedy is seeking to address the whole of the AEC we say this is a proper approach that is being taken here.

PROFESSOR PICKERING: Is it addressing the whole of the AEC? It is intended to address the problem of further growth of concentration in a specific defined set of market situations. It is intended to facilitate a response to another aspect of the AEC, and I think part of Mr. Green's concern is that the probability of the benefits arising from the facilitation is not actually being explored in any depth. Therefore, the costs may well be exceeding the likely benefits at least in that respect. Have we got an incomplete test here?

MR. ROTH: We say no, because, first of all, the costs that he suggests, which are the unmet demand costs – I think that is what is being said to be the costs, not the costs that are quantified and looked at in the Report, it is said to be these other costs resulting from unmet demand – do not realistically arise because of the way, in fact, the market will respond and the safety valve as well. We say, and here is the point, that over time it will be addressing the whole of the AEC through the change in the circumstances in the market place. That is how it plays out.

PROFESSOR PICKERING: Thank you. I hear what you say on that. Perhaps I might just offer the observation that, as you will have gathered from my questions to Mr. Green this morning, I wonder about the economic and business realism of the concept of unmet demand that is addressed in the report. I do not know whether you had it in mind to offer us some observations on that from your perspective at some stage in your submissions, but if you did have that in mind I would be interested to hear.

MR. ROTH: I most certainly will. I think, but I will be corrected if I am wrong, that "unmet demand" is not an expression that is used in the report. It certainly does not feature significantly. It has been put in a lot in this case. I will come back to that point.

THE PRESIDENT: Are you going on to look at other bits of this document?

MR. ROTH: I was going to look at the basis on which it has been argued that we should have carried out this more detailed assessment, the quantitative or qualitative or mixture, of which I think there were four. There was the case before the Commission on appeal from

the Gas and Electricity Markets Authority, there was *Vodafone*, there were the Ofcom guidelines and there was the Green Book.

THE PRESIDENT: At some point it may be that you want to say something about what these guidelines say on the effectiveness of remedies and the choice of remedies. That is paras.4.13 through to 4.25, not now but at some point.

MR. ROTH: Yes, certainly. I wanted to turn in the same bundle to the *E.On v. GEMA* case which is at tab 9. This was a rather unusual case under the regime. The Competition Commission was sitting as an appellate body, not something that it often does. This concerned the proposals of the Gas and Electricity Markets Authority, the GEMA, to modify the uniform network code governing the off-take of gas from the national transmission system. Their powers were being exercised under the Utilities Act of 2000, it is s.5A, and one sees that in para.2.20, p.4:

> "Under section 5A of the Utilities Act 2000 where GEMA is proposing to do anything for the purposes of, or in connection with, the carrying out of any function under Part 1 of GA86, and it appears to GEMA that the proposal is important according to certain criteria, GEMA must either carry out and publish an impact assessment or publish a statement setting out its reasons for thinking that it is unnecessary to do so. Where GEMA publishes an impact assessment, it must provide an opportunity for interested persons to make representations in response to it. The requirement for an impact assessment does not apply where a matter is urgent."

GEMA, accordingly, as required, did carry out an impact assessment, and one sees that at 2.61 on p.11:

> "On 7 February 2007, GEMA published a Final Impact Assessment in relation to proposal 116V …"

and the point of the passage in this appeal decision on which Mr. Green relied was that the Competition Commission on the appeal process was there dealing with the criticisms which were directed at the impact assessment which the GEMA had carried out as it was mandated to do, and that is the passage on p.48. 6.157, it is the paragraph he relied on, about what that impact assessment must comprise. That is the *E.On v GEMA* case.

The *Vodafone* case under the next tab, 10, was an appeal against a decision of Ofcom to modify the general condition that applied to mobile network operators in respect of their obligations regarding number portability. So again this was a regulator's modification to an existing regulatory process – that is what had happened – and it was a modification that

required an impact assessment, under the Communications Act 2003, s.7, which is set out in para.14 of the judgment on p.9:

> "OFCOM are also under a duty, in certain circumstances, to carry out impact assessments under section 7 of the CA 2003."

and that is a specific duty to carry out impact assessments, and if you look across the page s.47 of the Act, that is a quite separate and specific duty from s.47 which has a general requirement of proportionality in subsection 2(c) – tests for certifying or modifying conditions. Do you have that?

THE PRESIDENT: Yes.

MR. ROTH: You see at 2(c) there is general proportionality, but there is also overlaid on that a specific requirement in s.7 to carry out impact assessments. So, of course, Ofcom did carry out an impact assessment and this was an appeal on the merits, not a Judicial Review, a full appeal on the merits, and in examining the impact assessment which Ofcom had carried out this Tribunal held that they had not carried it out to the requisite standard (para.126) in the decision.

125 refers back to the *GEMA* case and the second sentence says:

> "While adopted under the specific statutory framework laid down in the energy Act 2004, we agree with the CC's approach to analysing a regulator's assessment of the costs and benefits of a proposed modification to existing processes."

That is existing regulatory processes.

> "126 In considering the CBA as a whole, the Tribunal finds that it was not carried out to the requisite standard and does not withstand the level of scrutiny which we are required to apply under section 195 of the CA 2003."

- and that is being a full merits appeal to the Tribunal.

MR. MATHER: Just on existing processes are you drawing a distinction there between modifying the planning process or recommending that, and the matters you have been describing?

MR. ROTH: Yes, because these are regulatory processes that have been imposed under this legislation or the other legislation that was there applied, as a regulation of the way the mobile network operators, or the gas people, carrying out their business, they were subject to that regulatory scheme, general conditions, and there was a modification to that scheme under the regulatory umbrella.

We say that neither the *Vodafone* case nor the *GEMA* case tell one really anything at all about whether an impact assessment is required of the Competition Commission in

carrying out its statutory duties under the Enterprise Act, save only for this, both these cases show that where a regulator is required to carry out an impact assessment that is now expressly set out in the governing statute by particular provision – it is particularly striking in the Communications Act because there is a general proportionality provision, but still there is this additional provision saying such an assessment is required. It is not left to be implied under some general principle of proportionality – a principle that applies to all regulators under the general law and yet that is what is being contended for here.

THE PRESIDENT: Well I think it is being said it really is implicit in, as comprehensive as possible, and reasonable and practicable that encompassed in that you have really got to look at all these things.

MR. ROTH: Yes, absolutely. "Comprehensive" is the solution to the AEC, but it is said that reasonable and practicable encompasses by implication a requirement to carry out this sort of impact assessment.

THE PRESIDENT: But what is it that you do not have to do that this would require you to do? What is the real difference that is relevant to our case. You are recommending a pretty drastic kind of across the country remedy that will actually limit how much people can do by way of business expansion and so on in 24 per cent of large stores apparently. So it is intended to have a cross the country effect. You would expect therefore, would you not, that you would adopt as best practice some pretty rigorous assessment of what its effects and costs and benefits and all the rest of it would be. Why should you be subject to any lesser approach? I am just interested to know what difference it is going to make.

MR. ROTH: What I am resisting is the suggestion that it has to be this rather formalised process that is involved in the kind of exercise ----

THE PRESIDENT: Yes, I think Mr. Green backed off a bit in the end from saying that it was a formalistic requirement, I think he ended up saying it was just something you would have to do rather than have to do it in any particular way but that these questions would need to be answered.

MR. ROTH: Well you have to think about what effect your remedy is going to have and you have to think about what cost it will impose ----

THE PRESIDENT: Exactly.

MR. ROTH: -- upon the people who are subjected to it, and we say – and I will come to the proportionality section – that that is what the Commission in fact did. But it has to go further and try and work some calculations of saying: "Well, of the 24 percent of existing stores, how many of those might have sought to expand in the absence of a competition

test? Of those that might have sought to expand, in how many of those areas would a new rival then come in?" That is the first element. Secondly, how many areas might a new store have been built to try and -- Where might it be so that you can draw an isochrone around it, and say, well, is it a concentrated market such as the test would bite, or not? It is not straightforward.

THE PRESIDENT: No. But, he says you have got a lot of information.

MR. ROTH: He does. I shall deal with that. I say, indeed, not only that, but it becomes an exercise that cannot meaningfully be done to produce any sensible answer that can be applied to it. As I say, I shall come back to that under my last heading. If it is right that it has to be done, it has to be done, of course, not just for the competition test - though that is the focus of these proceedings - but it has to be done for the controlled landsites remedy. It has to be done for the code of practice with regard to suppliers, which is another remedy you would have seen from the report that one did not do. Indeed, it would have to be done on that basis on merger remedies in merger cases. It has therefore very far-reaching implications for the Commission as to the sort of work it has to carry out in these cases.

THE PRESIDENT: It might depend upon whether things are self-evident or not, might it not? It all depends, I think is the answer. If something is admittedly not having any direct effect on anything, and it is going to have another kind of effect -- It may be that one has to look more closely than if the effect is obvious.

MR. ROTH: We say the effect is obvious, but one then gets to, "Well, what is the scale of the effect set against the costs?" The controlled landsites - it is freeing them up for other development. Again, you have got to start estimating to what extent it will take place. Sometimes it can be done more easily. Sometimes it is extremely difficult. Sometimes it cannot be meaningfully done.

THE PRESIDENT: One thing we do know here is that there is a vast amount of very detailed work that has been done by the Commission and others on their behalf.

MR. ROTH: The question is whether that, in looking to the future, enables one to make sensible estimates. That is something that I will come to.

MR. MATHER: Just before leaving that point, can you help us -- Is there a public policy rationale for the distinction between the tighter regime which applies in the circumstances you have described and the greater flexibility you are telling us that the Competition Commission has? Is it because there is a narrower, more economic task in the first set of cases?

MR. ROTH: I think the rationale, in a way, is best highlighted by the passage at the beginning of the Green Book saying what sort of endeavour - trying to use a neutral word - or activity that kind of exercise should be applied to. The Green Book is in Bundle 4 of our bundles, which is Bundle 6 of your bundles at Tab 76. This is the Treasury Green Book. Within the book at p.2 (which is stamped p.3192) - 'When to use the Green Book'. One starts above - 'Activities covered by the Green Book'.

> "Policy and programme development - Decisions on the level and type of services or other actions to be provided, or on the extent of regulation.
>
> New or replacement capital projects - Decisions to undertake a project, its scale and location, timing, and the degree of private sector involvement.
>
> Use or disposal of existing assets - Decisions to sell land, or other assets, replace or relocate facilities or operations, whether to contract out our market test services.
>
> Specification of regulations - Decisions, for example, on standards for health and safety, environment quality, sustainability, or to balance the costs and benefits of regulatory standards and how they can be implemented.
>
> Major procurement decisions - Decisions to purchase the delivery of services, works or goods, usually from private sector suppliers.
>
> When to use the Green Book - The Green Book will be useful for: Anyone required to conduct a basic appraisal or evaluation of a policy, project or programme; and people seeking to expand their knowledge in this area.
>
> The guidance applies: *At the start* ... to any analysis used to support a government decision to adopt a new policy , or to initiate, renew, expand or re-orientate programmes or projects, which would result in measurable benefits and/or costs to the public. This is the appraisal part of the process.
>
> *And at the finish* ... to retrospective analysis of a policy, programme or project at its completion, conclusion or revision. This is the evaluation part of the process".

The difference with all that from s.134 is that there you have a situation where you start by looking to see - and have to look to see - if there is an adverse effect on competition. Then, if you find there is an adverse effect on competition - then you pick up my submissions right at the start - you have to go about finding an appropriate remedy for it, or a reasonable remedy for it. So, it is not an initiation or a replacement, or a decision of the kind taken here when you say, "Is there something that is worth embarking upon, or should one do nothing?"

THE PRESIDENT: I think Mr. Green took us to s.3 - the reasons for government intervention. Market failure, and so on.. It looks as though it is not covered in its preamble, as it were, but there may be interesting areas of analogy, at any rate. Government intervention can incur costs, and so on, and so forth -- Paragraphs 3.2 and 3.3. I think that was the bit that he was looking at at one point.

MR. ROTH: Yes. 3.1 is, of course, is the introduction.

> "Before any possible action by government is contemplated, it is important to identify a clear need which it is in the national interest for government to address".

You start saying, "Is there actually a need to go and do anything at all? But, here we have a situations where, under the Act, once you find the AEC you are effectively, save in that theoretically possible, but in reality highly unlikely, situation, required to come in with an appropriate and reasonable remedy. Now, if it is another case of market failure, one could say, "No, better do nothing about it" because the remedy causes more disruption or distortion to a market than all your are trying to cure. Was it Victor Bork who said that his father, a chemist, developed a cure for which there was no disease? (Laughter) One wants to avoid that.

Back in the authorities bundle - and this goes very much to the same point - Why do those guidelines apply to Ofcom in this situation? - at Tab 22, para. 1.1 goes to the question that is being asked,

> "Why is Impact Assessment important? The decisions which Ofcom makes can impose significant costs on our stakeholders and it is important for us to think very carefully before adding to the burden of regulation. One of our key regulatory principles is that we have a bias against intervention. This means a high hurdle must be overcome before we regulate. If intervention is justified, we aim to choose the least intrusive means of achieving our objectives, recognising the potential for regulation to reduce competition. These guidelines explain how Impact Assessments will be used to help us apply these principles in a transparent and justifiable way."

They are on the background where there is a bias against intervention and you carry out the assessment to see, is there a basis on which intervention can be validated? That is not the approach of s.134 of the Enterprise Act. When you have found an AEC there is not a bias against doing anything about it. On the contrary, the whole thrust of s.134 is that you must

do something about it. You must come up with a solution. That is why I say these assessments are dealing with a different governmental or public authority scenario.

One asks, what did the Competition Commission do here and was proportionality correctly applied? They looked at the scale of the adverse effect on competition when asking, is the remedy proportionate. That was substantially on just the two elements of the existing effect – the local effect in terms of the PQRS, which was estimated at £105-£125 million per year, and the effect on national pricing which they said was difficult to measure, but potentially very substantial. They explain that on the basis of saying, even it is very small in relative terms, it will translate into a significant sum in actual terms. I find it very difficult to work out what it actually is, but even if it is only 0.1 per cent that will have an effect of £80 million per year.

Although there are challenges in the witness statements from Tesco to those passages, they are findings in the report that Tesco does not seek to quash. As against that, the Commission looked at the burden or the cost of the remedy on those who would be subjected to it. That is Chapter 11 in the Report, which is at 11.377 under the heading of "Proportionality". 11.377:

> "In discussing each element of our package of remedies above, we have taken care to ensure that our chosen remedies represented the least-cost, least-intrusive package that would be effective in addressing each of the AECs we found."

Again reflecting s.134.

> "We are satisfied that our remedies to address the AEC we found in relation to highly concentrated local markets rep the least-cost, least-intrusive package that would be effective."

Then they refer to the difference over the Ombudsman.

Then they turn in 11.379 to the position in highly concentrated local markets. They look at the scale of the adverse effect, the costs associated with each of the components and the scope of the remedy. 11.380 looks at the scale of the effect that I have just explained, and then at 11.381 they note the different components of the remedy and set out the costs for each of them.

Then 11.382 starts on the competition test. They deal with implementation costs, and they do note at 11.385 the submission from Tesco that the test would cost very much more:

> "The great majority of these costs comprise delay costs to retailers and consumers."

They set out Tesco's estimates of costs that Tesco put them in table 11.2. They explain how the delay costs have been calculated by Tesco in 11.386, that it would add two weeks to the planning process and each appeal would take 12 months. They evaluate that in considering, is that delay cost effect on consumers likely. In 11.387 they come to the view it will not result in more time being required to consider planning applications. We say that that is a judgment they are fully entitled to make, and within their sphere of judgment that the Commission can make. So on that basis they do not think that it will have that effect on either the retailers or the customers. They come down to the retailer's costs which Tesco put at £9.5 to £12 million a year. Then they examine that in 11.389 and they come to the figure of £5 to £6 million.

They also say, I should say, at 11.388:

> "Tesco also assumed that appeals arising from the competition test would delay store openings. As discussed in para.11.122, we do not regard the scope for challenge as high, and we do not consider that the competition test will significantly increase the time taken for planning applications to be determined."

Again, that is a view that they are fully entitled to come to, and indeed I do not think 11.122 – I will be corrected if I am wrong – is one of the findings that Tesco is seeking to quash.

So they look at effect on consumers and retailers as costed by Tesco and say, no, they do not find those costs, but they do find part of the other costs. We say that judgment is well within the margin of appreciation when they look at the compliance costs.

On that basis they conclude that this part of the remedy is proportionate and we say that is an entirely orthodox analysis in applying proportionality in accordance with their guidelines, looking at the scale of the problem they are addressing and then saying, "Is the effect both in terms of burden and effect on others in the market, including the consumers out of proportionate to the objective that we are addressing?"

I see that it is just 4.30.

THE PRESIDENT: Mr. Roth, you are still on target, are you, for, do you say, mid-morning?

MR. ROTH: Yes.

THE PRESIDENT: We are going to start at ten, if that is convenient. Thank you very much.

(Adjourned until 10.00 am on Thursday, 13th November 2008)