

OFT v IBA Health Limited¹

“A New Regime Emerges?”

By Ben Lask
February 2004

Summary

1. On 19 February 2004 the Court of Appeal handed down judgment in *OFT v IBA Health* – the first case to consider the new merger control regime established by the Enterprise Act 2002 (“the Act”).
2. Under the new regime the OFT replaces the Secretary of State as the body with responsibility for referring mergers to the Competition Commission (“the Commission”). Whereas the Secretary of State had a discretion to refer, the OFT has a duty; and the previous “public interest” test for whether a reference should be made is replaced by a “substantial lessening of competition” test. Decisions of the OFT or Competition Commission relating to the merger control regime are subject to review by the CAT under a new power conferred by s.120 of the Act.
3. In December the Competition Appeal Tribunal (“CAT”) had quashed the OFT’s decision not to refer the merger between iSoft Group plc (“iSoft”) and Torex plc (“Torex”) to the Commission and remitted the matter for reconsideration. Apart from criticising the terms and content of the OFT’s decision it had said that the test for reference was not that applied by the OFT. It had also rejected reference to ordinary judicial review case law on the basis that it was a specialist tribunal. The OFT and the merging parties appealed to the Court of Appeal. The OFT was concerned about two important issues of principle: (i) the correct interpretation of s.33 of the Act (the duty to refer); and (ii) the scope of the CAT’s new review function under s.120.
4. The Court of Appeal rejected the approach of the CAT and has given a new interpretation of the s.33 reference test. Further, the Court confirmed that ordinary principles of judicial review apply in the CAT in the same way that they would in the Administrative Court, although those principles are themselves flexible.

Background

5. iSoft and Torex were both engaged in the supply of IT software and systems to the healthcare market, in particular the supply of Electronic Patient Records and Laboratory Information Management Systems. Their combined share of these markets

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¹ Office of Fair Trading and Others v IBA Health Limited [2004] EWCA Civ 142

was, at the relevant time, 44% and 66% respectively. On 23 July 2003 iSoft offered to acquire the issued share capital in Torex and the proposed merger was notified to the OFT on 1 August 2003. A relevant merger situation arose and the question was whether the OFT should refer it for an in-depth investigation by the Competition Commission pursuant to s.33. Section 33(1) provides:

The OFT shall, subject to subsections (2) and (3), make a reference to the Commission if the OFT believes that it is or may be the case that –

- (a) arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation; and*
- (b) the creation of that situation may be expected to result in a substantial lessening of competition within any market or markets in the United Kingdom for goods or services.*

6. In a decision dated 6 November 2003 running to 34 paragraphs the OFT decided not to refer the merger. It accepted that in terms of their “legacy” contracts - in respect of existing IT systems - iSoft and Torex were the two leading suppliers of IT software to the UK healthcare sector. But the effect of the merger on competition in the sector had to be viewed in the light of the National Programme for IT (“NPfIT”) – a huge new Department of Health programme designed to update NHS IT systems. The NPfIT fundamentally altered the future competitive landscape and meant that competitive constraints had to be viewed under a new scenario. For example, the £2.3bn increase in funding under the NPfIT had attracted bids from major international competitors which made it likely that competition for future contracts would remain active. Accordingly the OFT did not believe *“that it is or may be the case that, if carried into effect, the creation of this relevant merger situation may be expected to result in a substantial lessening of competition within any market or markets in the United Kingdom for goods and services”*.
7. Subsequently IBA Health Limited (“IBA”), an Australian producer of healthcare IT systems, applied to the CAT for a review of the OFT’s decision under s.120 of the Act. IBA complained that the OFT had erred in concluding that the duty to refer did not arise; and had failed to conduct an appropriate or adequate investigation before adopting the decision.
8. Section 120 of the Act provides:

(1) Any person aggrieved by a decision of the OFT, the Secretary of State or the Commission under this part in connection with a reference or possible reference in relation to a relevant merger situation or a special merger situation may apply to the Competition Appeal Tribunal for a review of that decision.

...

(4) In determining such an application the Competition Appeal Tribunal shall apply the same principles as would be applied by a court on an application for judicial review.

CAT Proceedings

Correct interpretation of s.33(1)

9. In construing s.33(1) the CAT reviewed the statutory framework of the Act and considered that the key issue was as to the intended balance between the OFT and Commission stages of inquiry. Of particular contextual importance was the OFT’s role as a “first screen” whereby it was tasked to carry out no more than a preliminary investigation.
10. The CAT considered that the phrase *“is or may be the case”* in the opening part of s.33(1) was central to the appeal. The inclusion of “may” indicated that where there was “room for two

views" on the question whether the merger may be expected to lead to a substantial lessening of competition ("SLC") the duty to refer arose. As to whether a merger gave rise to "room for two views" the CAT formulated a two-limb test. The OFT had to satisfy itself (i) that as far as it was concerned there was no significant prospect of a SLC; and (ii) that there was no significant prospect of an alternative view being taken in the context of a fuller investigation by the Commission.

The scope of the CAT's review function

11. The CAT said that it found it difficult to interpret the duty imposed on it by s.120(4). Nonetheless it proceeded on the basis of a number of propositions. First, the principles to be applied on an application for judicial review varied with the particular context. Secondly, since the CAT was a specialised tribunal, the reasoning of Administrative Court decisions on judicial review of regulators was not directly applicable. Thirdly, since unlike *Wednesbury* this case concerned review of a statutory duty, a test geared towards controlling a discretionary power was not appropriate. Fourthly, the CAT's task was primarily to decide which of two other specialised decision makers, the OFT or the Commission, should take the decision. And fifthly, the broad question the CAT asked itself was whether it was satisfied that the OFT's decision was not erroneous in law, and was one which it was reasonably open to the OFT to take, giving the word "reasonably" its ordinary and natural meaning.

Conclusions of the CAT

12. In respect of the two-limb test under s.33(1), the CAT found that the OFT had failed to consider the second limb. Further, the decision failed to set out either the facts upon which it was based or the material the OFT had relied upon. Accordingly, the CAT could not be satisfied that all material considerations had been taken into account, nor that there was material upon which the OFT could reasonably have reached its conclusion.
13. The CAT thus quashed the OFT's decision not to refer and directed that it reconsider the matter. The OFT and the merging parties appealed on the basis that both the test adopted by the CAT under s.33(1) and the CAT's approach to its own review function under s.120(4) were erroneous.

Court of Appeal Proceedings

Correct interpretation of s.33(1)

14. Agreeing with the appellants, the Court firmly rejected the CAT's two-limb test. The belief required by s.33(1) in order to trigger the duty to refer was the OFT's belief that the merger may be expected to result in a SLC, not that the Commission may in due course reach such a view. Were the CAT's test correct, comparable provisions in the Act, which also used the phrase "*is or may be the case*", would become unworkable. For example, the absurd situation would arise whereby the Secretary of State's own jurisdiction to refer a merger to the Commission under s.45 would depend on the OFT's belief as to what the Commission might decide.
15. So what was the correct test? Precisely that stated in s.33(1). The words were ordinary English words and should be applied in accordance with their ordinary meaning. Giving the lead judgment, the Vice-Chancellor warned against attempts to paraphrase or gloss the words used in the statute. In particular, despite having earlier advocated a degree of deference to the OFT's own published interpretation of s.33(1), he found that it effectively substituted "significant prospect" for "may" and was therefore open to criticism as setting the requisite degree of likelihood too high.
16. That said, in recognition of the many possible meanings of "may", the Vice-Chancellor sought to elucidate the statutory test. First, in order for the duty to refer to arise, it was necessary for the OFT to form the relevant *belief* that the merger may be expected to result in a SLC; a mere suspicion was insufficient. Secondly, that belief must be reasonable and objectively justified by

the relevant facts. And thirdly, the degree of likelihood required by the word “may” in the phrase “*is or may be the case*” was higher than fanciful but lower than 50%. In between those two extremes the OFT had a wide margin in which to exercise its judgment.

17. Lord Justice Carnwath agreed with the Vice-Chancellor and in a separate judgment he reached a slightly different view from the CAT as to the respective roles of the OFT and the Commission. The statutory framework suggested that the formation of a *belief* in the possibility of SLC by the OFT required more than just a preliminary investigation. For example, under ss.44-46, the OFT’s belief as to SLC was treated as a decision binding on the Secretary of State. This, together with the OFT’s expertise, pointed towards something more than a purely first-screen role. However, sharing the Vice-Chancellor’s reluctance to qualify the statutory wording, he declined to express precisely what that “something more” involved.

The scope of the CAT’s review function

18. The Vice-Chancellor agreed with the appellants that s.120(4) imposed upon the CAT a mandatory requirement to apply the ordinary principles of Judicial Review. But he declined to criticise the CAT and held that it had neither reversed the burden of proof nor erred in failing to apply the *Wednesbury* test of unreasonableness. As to the latter it was plain that unreasonableness in the ordinary and natural sense of the word differed from *Wednesbury* unreasonableness. However, he concluded that a proper reading of the CAT’s judgment revealed that it had not adopted the wrong standard of unreasonableness when seeking to apply the *Wednesbury* test.
19. Lord Justice Carnwath added that, although the CAT’s approach to review should, as it suggested, reflect the specific context, this did not permit it to discard established administrative case-law relating to “reasonableness” in favour of the ordinary and natural meaning of that word. Moreover this was unnecessary since the ordinary principles of Judicial Review were flexible enough to be adapted to the particular statutory context.
20. Further the CAT’s concern at having to consider material outside the OFT’s decision letter was misplaced. The OFT’s statutory duty to give reasons (s.107) was important but there was no statutory requirement for all the evidence to be set out in the decision letter. Accordingly there was nothing unusual in the OFT’s written reasons being amplified by evidence before the Court.

Conclusions of the Court of Appeal

21. As to the deficiency of the OFT’s reasoning, the Court agreed with the CAT. The OFT’s conclusions failed to discount the likelihood of a SLC. Further the conclusion that the NPfIT altered the future competitive landscape was insufficient to justify the further conclusion that existing anti-competitive features, including the parties’ market share, were overcome, such as to remove the requisite likelihood of a SLC. Therefore either the OFT had applied too high a test of likelihood when forming its belief as to whether the merger may be expected to result in a SLC, or it failed adequately to justify the belief it formed in accordance with the proper test. Either way, and notwithstanding the mistaken adoption of the two-stage test under s.33(1), the CAT’s ultimate conclusion was right and should be upheld.
22. Lord Justice Mance concurred with the judgments of the Vice Chancellor and Lord Justice Carnwath. iSoft’s application for permission to appeal to the House of Lords was refused. The OFT did not seek permission to appeal.

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The OFT was represented in the Court of Appeal by Peter Roth QC and Daniel Beard of Monckton Chambers.