

## The Groceries Market Investigation (Controlled Land) Order 2009

### Response to consultation

#### Introduction

1. We received nine responses to our formal consultation on the draft Order, published on 28 April 2009.<sup>1</sup> We have taken these submissions into account and have now issued an amended draft Order for further consultation. In this paper we summarize the changes of substance made to the draft as a result of submissions accepted and give reasons for rejecting other submissions. Very minor changes are not discussed. Consequential amendments to the explanatory note have been made following the changes made to the draft Order.
2. Unless the context implies otherwise, references below to articles in the Order refer to articles in the revised Order.

#### Changes made

##### *The Order*

##### *Article 2*

3. We have added definitions of 'Access Road', 'Car Park', 'Operational Land Restriction' and 'Service Yard' (see paragraphs 24 to 28).
4. We have amended the definition of 'Exclusivity Agreement' so that it applies to any person with an interest in the land the subject of the exclusivity agreement, rather than merely the owner of the land.
5. We have added a definition of 'Implementation Date' (see paragraphs 15 and 21).
6. We have included a definition of 'Interconnected Bodies Corporate', which is consistent with the Enterprise Act 2002 (the Act) (see paragraph 35) and 'Pension Company' (see paragraph 29).
7. We have clarified the definition of 'Restrictive Covenant' so as to ensure that it is mutually exclusive from the definition of 'Exclusivity Agreement'.
8. We have replaced the word 'tenant' with 'lessee' in the definition of 'User Clause' to reflect that a tenant need not always be a leaseholder.

##### *Article 3*

9. We have amended the acquisition provision in Article 3(2) to provide that a person must acquire all or substantially all of the 'Groceries retailing' business of a retailer in order for them also to be a Designated Retailer. This better reflects the focus of the Order on grocery retailing.

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<sup>1</sup>This follows an earlier informal consultation with a large number of parties, which informed the initial drafting of the Order.

10. We have amended Article 3(4) so that it is sufficient to meet the criteria to become a Designated Retailer if a grocery retailer has operations throughout a 'considerable part' of Great Britain and Northern Ireland. The purpose of this amendment is to allow for designation of those retailers that have an extensive geographical network across a number of regions but that, for various reasons, may not have a presence throughout the whole of Great Britain and/or Northern Ireland.
11. We have amended the criteria requiring a retailer to provide 'a full range of groceries' in order to be designated. One respondent noted that a retailer need not carry all of the products described in the definition of 'Groceries' to be regarded a grocery retailer. We have therefore amended the criterion to read 'a range of groceries'. As set out in Article 3(3), the Office of Fair Trading (OFT) retains discretion as to whether a retailer should be designated for the purposes of the Order.

#### *Article 4*

12. We have amended this Article so that its obligations apply to all retailers designated under the Order, not just to those retailers designated on commencement.
13. We have amended Article 4(3)(b)(i) so that the permitted restrictions in Article 6 apply (see paragraph 20). We have also amended Article 4(3)(b)(ii) so that it applies to all restrictive covenants which are 'enforceable' by Large Grocery Retailers as a retailer may still be able to enforce a restriction even after it has sold the land to which it applies.
14. We have included a long stop date for the time period to be specified by the OFT, where it requires a retailer to procure the removal of a restrictive covenant in the circumstances set out in Article 4(4).
15. We have included a separate implementation date for the mechanism by which parties can apply to the OFT to have a restrictive covenant released. This will allow the OFT to obtain the software and establish the procedures necessary to carry out the Test set out in Schedule 4.
16. One respondent submitted that, on application by the owner of land benefiting from a restrictive covenant, the land registry would not usually remove entries from the register, but merely add a note to the register to record that there is a purported release. They suggested an alternative mechanism whereby retailers should be required to (i) enter into a unilateral deed of release and (ii) use reasonable endeavours to procure the removal of the covenant from the register (since this should be sufficient to ensure that the registry notes on the register that there has been a purported release). We accept that there may be difficulties requiring the removal of restrictive covenants from land registers. However, we continue to believe that an agreed deed of release with the owner of the burdened land is appropriate. An agreed release, as opposed to a unilateral release, will bind successors in title of the land benefiting from the restrictive covenant. We therefore believe that this is the most effective mechanism for releasing restrictive covenants.
17. In response to this submission, and other related submissions, we have amended Article 4 to provide that in the event that a retailer cannot, despite its best endeavours, procure that a restrictive covenant is removed from the relevant register in accordance with Article 4(1)(b) it will:
  - procure the noting of the attempted removal on the appropriate register;
  - execute a declaration providing that it will not enforce the restrictive covenant; and

- ensure that any successors in title of the land benefiting from the Restrictive Covenant sign a similar declaration.
18. The Order includes a list of restrictive covenants which were found to prevent, restrict or distort competition. One of these restrictive covenants (in Oundle, Cambridgeshire) is for the benefit of Midlands Co-operative Society Limited, which will not be a Designated Retailer at the commencement of the Order. Article 4(7) therefore imposes an obligation on Midlands Co-operative Society Limited to release the Oundle restrictive covenant.
  19. A number of respondents submitted that the 'best endeavours' clause should be amended to 'all reasonable endeavours' to avoid situations where the attaining of the release of a restrictive covenant would require a retailer to reimburse parties whose consent is required to any such release. We have added to the Order a clarification that 'best endeavours' does not include an obligation to make payments to procure parties to consent to any release.

### *Articles 5 and 6*

20. We have split Article 5 of our previous draft into two distinct articles to allow for the permitted restrictive covenants (for residential leases and user clauses) to apply to both existing and future restrictive covenants (with the exception of those covenants identified in the Groceries market investigation [final report](#) (the Report) as preventing, restricting or distorting competition). We have also amended Article 5(1)(c) so that the procurement clause is consistent with Articles 5(1)(a) and 5(1)(b).

### *Article 7*

21. For similar reasons to that set out in paragraph 15, we have included a separate implementation date for the mechanism by which parties can apply to the OFT to have an exclusivity agreement released.
22. We have amended Article 7(2)(b)(ii) to provide that Exclusivity Arrangements need only benefit land 'used by' Large Grocery Retailers, to reflect the fact that many grocery stores are built on land leased by the relevant retailer, rather than owned by it.
23. We have amended the time period following which retailers must not seek to enforce exclusivity arrangements (Article 7(4)(a)) to better reflect the time periods set out in the Report.

### *Article 9*

24. A number of retailers suggested to us that the prohibition on restrictive covenants and exclusivity arrangements would create practical difficulties regarding amenities that were essential for the operation of individual stores. The Order published for the first formal consultation contained an exception for restrictions regarding land adjacent to a store (and not owned by the retailer) being used as a car park. A number of respondents to the consultation requested that this exception be expanded.
25. Submissions on the extent of any expansion differed among retailers, but varied from a limited expansion for land required for the operation of the store, to allowing standard user clauses and restrictions on mixed-use developments owned by the retailer. We carefully considered each submission. However, we remain concerned that allowing all user clauses could allow retailers to circumvent the Order by entering

into a long-term lease that a property must be used in a particular way (other than grocery retailing). In addition, we do not consider it consistent with the findings in the Report to allow retailers to impose restrictive covenants on mixed-use developments, and we do not consider that there are special reasons to depart from the Report in this respect.

26. There were various submissions on restrictions that may be required for the effective operation of a grocery store. One retailer provided examples of access roads and service areas that were on land that was not owned by the retailer, but were required to be set aside for the retailer to use in order for the store to operate, while another provided a more general example of restrictions relating to the maintenance and configuration of a mall and its facilities. We have attempted to balance the need for effective operation of grocery stores with the need to be consistent with the Report and restrict any possible avoidance of the primary obligations in the Order.
27. We have therefore adopted a narrow exception for certain categories of land that are necessary for the operation of a grocery store. A new Article 9 provides that the obligation in Article 4 and the prohibitions in Articles 5, 7 and 8 will not apply to 'Operational Land Restrictions'. 'Operational Land Restrictions' are restrictions which prevent land from being used other than for car parks, service yards or access roads, and which are essential for the effective operation of the relevant grocery store. The exclusion will only apply to land not owned by the retailer, which is adjacent to the relevant grocery store, and which is not subject to an existing planning condition or planning obligation regarding its use as a car park, service yard or access road. To ensure that the exception is not used to restrict the activities of other grocery retailers (or potential entrants) in multi-store developments, the restriction will not benefit from the exception if it provides for exclusive use of land to the exclusion of other grocery retailers.
28. It was submitted by some retailers that the presence of an existing planning condition or planning obligation would not protect the retailer, as planning restrictions are subject to change by the relevant planning authority. However, we consider that the presence of a planning obligation provides sufficient protection for retailers in such circumstances, and that a retailer will have the opportunity to contest any proposed change to a planning obligation.

#### *Article 10*

29. We have included a limited exception for land owned by retailer's pension companies. It was submitted to us that pension companies have significant land holdings which are unrelated to their grocery operations, and that the remedy should not restrict these activities. It was noted that pension companies are required to operate independently to maximize the value of the pension fund. We consulted with a number of retailers specifically on this issue, which noted that some retailers' pension companies now hold property that is leased back to the retailer for its use. In addition, some retailers cautioned against a wide exception which could be used to avoid the effects of as an avoidance mechanism.
30. After careful consideration of the various submissions, we have included a limited exception for pension fund companies. The exception would allow pension fund companies to enter restrictive covenants and exclusivity arrangements (which they would not be able to do without the exception), except to the extent that:
  - (a) the restriction relates to land which the retailer uses (or has used) as a grocery store; and

(b) if the restriction is in a highly concentrated area and the grocery retailer is the strong incumbent, a third party can apply to the OFT to have the restriction lifted (ie a similar mechanism to that which already exists).

31. This would allow pension fund companies to enter into restrictions that do not relate to the parent company's grocery retail business, while allowing competing retailers or local councils to apply to lift any restrictions in highly-concentrated areas if necessary. We realize that there are likely to be some restrictive covenants and exclusivity arrangements that are not aimed at protecting the retailer's grocery retailing business but that are in highly-concentrated areas. However, we believe that this limitation to the exception is necessary to prevent avoidance. We note that some retailers consulted submitted that no exception was necessary, as their pension funds investments were of such a nature that they would not be affected by the Order.
32. We received a submission that a similar exception to that for pension funds be given in respect of the insurance operations of Co-operative Group Limited (CGL). CGL submitted that its insurance business held investment funds for the benefit of policyholders, and that the Order would frustrate the bona fide business of its insurance subsidiaries. The CC considered carefully the submission provided by CGL. However, we were not convinced that the insurance operations were sufficiently independent of the grocery retail operations of CGL, nor were we provided with sufficient examples of how the Order would affect CGL insurance operations. Therefore, we have not included an exception for these businesses in the Order.

#### *Article 11*

33. We have included a requirement for Large Grocery Retailers to notify the OFT if they acquire a Large Grocery Store. This is consistent with the CC's Groceries Remittal decision,<sup>2</sup> which recommended the adoption of the competition test, along with associated information requirements.

#### *Article 12*

34. We have included a reference in Article 12 to [section 109\(7\)](#) of the Act to make clear that the OFT cannot require parties to provide it with privileged information.

#### *Schedule 1*

35. We have amended the reference to subsidiaries in Schedule 1 to 'groups of Interconnected Bodies Corporate', consistent with the definition in the Act. In order to ensure that the Order applies to all companies that hold land on behalf of retailers, we have also included in the parties covered by the Order any companies that are controlled by the Large Grocery Retailers, their agents, or by any company in the same group of Interconnected Bodies Corporate. 'Control' is defined as having a shareholding of over 25 per cent of the voting rights in the other company, or having the power to appoint more than one quarter of its directors.

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<sup>2</sup>[Groceries Market Investigation: Remittal of the Competition Test by the Competition Appeal Tribunal](#) (2 October 2009), see paragraph 6.12, and paragraph 11.441 of the Report.

#### *Schedule 4*

36. We have adopted a number of suggestions made by the OFT to clarify the mechanism for the test to be applied pursuant to Articles 4 and 7. These include specifying that the test is passed if no relevant grocery store is identified in a 10-minute drive-time isochrone around the burdened site, and clarifying that stores under common ownership will be part of the same store fascia.
37. We have amended the market share threshold to provide that the test is failed if the market share is '60 per cent or greater', to ensure consistency with the proposed competition test.

#### *Schedule 5*

38. We have included a new schedule that will list the names of the pension companies of each Large Grocery Retailer.

### **Suggested changes not made**

#### ***General comments***

39. One respondent submitted that the 60 per cent market share threshold for the test in Schedule 4 was too high, and that a 50 per cent market share threshold was appropriate. However, the CC's reasoning for the market share threshold is set out in the Report, and was set after considerable debate. We do not believe that there are sufficient reasons to amend this market share threshold.

#### *Article 2*

40. Some respondents submitted that more detail be provided for the term 'significant proportion' in relation to the definition of 'Grocery Store'. One respondent suggested that a grocery store should be determined by its absolute size, rather than the proportion of the store dedicated to groceries. However, the Order takes the size of the store into account when applying the test in Schedule 4. In addition, the size of the grocery segment within a particular store will not generally be the sole factor in determining the significance of the grocery option. We have not made any changes to this definition.
41. One respondent submitted that 'Net Sales Area' should not include areas behind service counters. This area will generally not be covered by the definition, provided the area is not accessible to the customer. Another respondent queried whether the area was measured by all sales, or merely by grocery sales area. The definition will apply to all sales area. We have clarified this in the explanatory note.

#### *Article 3*

42. A number of respondents submitted that Article 3 should apply to all retailers with a strong regional presence, rather than merely national retailers. As set out in paragraph 10, we have amended the criteria for a 'Large Grocery Retailer' to include retailers with operations throughout a considerable proportion of Great Britain and Northern Ireland. However, the Report concludes that only large grocery retailers should be subject to the obligations regarding controlled land. We have therefore not amended the criteria to include grocers with a strong regional presence.

43. One respondent submitted that the term 'substantial' should be defined. However, given the various methods by which an acquisition of a grocery retailer may occur, we do not think that a definition of 'substantial' is appropriate in this case.
44. One respondent submitted that the Order should include a mechanism by which retailers could communicate to the OFT who should be a designated retailer under Article 3(3). However, we do not think that a formal mechanism is necessary for this purpose. Any person who believes that a retailer meets the 'Large Grocery Retailer' criteria can inform the OFT of this belief. It is then for the OFT to consider whether the criteria are met.

#### *Article 4*

45. Some respondents submitted that any person wishing to develop a site should be permitted to apply to have a restrictive covenant removed from that site. At present the Order (Article 4(4)) only allows for the land owner to request such a removal. We do not consider it appropriate for a restrictive covenant relating to a piece of land to be removed without the knowledge of the landowner. It is possible that the owner of the land may not want the restrictive covenant lifted (eg for tax reasons). If a party wishes to have an existing restrictive covenant lifted it has the option of agreeing this with the land owner. We have therefore not made any changes to the Order in response to these submissions.

#### *Article 5*

46. As set out in paragraphs 24 to 28, we received a number of submissions on the scope of the prohibition on restrictive covenants. The extent of the changes made, and the reasons for not accepting further changes, are set out in those paragraphs.
47. One retailer was concerned that the Order would prevent it from passing on restrictions which it had been forced to accept by previous landowners when acquiring land and which it must pass on in order to avoid exposure to legal action from the predecessor in title. The Order as published does not prevent retailers from acquiring a parcel of land benefiting from a restrictive covenant. However, enabling large grocery retailers to restrict the use of land they are developing is inconsistent with the purpose of the Order. We have therefore not made any amendments to the Order as a result of this submission.
48. One respondent submitted that the use of the word 'reflect' in Article 5(2)(b) was too vague and should be replaced with 'substantially reproduces any restriction on the use of land for the sale of Groceries contained herein'. However, we have not made any change to the Order as a result of this submission.

#### *Schedule 2a*

49. One respondent queried the 2000 cut-off date for the application of the prohibition on restrictive covenants set out in Schedule 2a. However, the restrictive covenants listed in this schedule are those that were notified to us during the inquiry. We also have a general procedure to be applied to restrictive covenants that were not considered during the inquiry, for which there is no such cut-off.

#### *Schedule 4*

50. One respondent submitted that the test should include a reference to the drive-time software to be used by the OFT and specified by the CC as a result of the drive-time consultation. However, the output of the CC drive-time consultation will be a recommendation only. The OFT will reach its own decision on the selection of appropriate drive-time software, applying any relevant procurement policies and rules.