Anticipated acquisition by Reckitt Benckiser of the K-Y brand from Johnson & Johnson – decision to refer

ME/6448-14

The CMA's decision on reference under section 33(1) of the Enterprise Act 2002 given on 7 January 2015. Full text of the decision published on 5 February 2015.

Please note that [✂] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

INTRODUCTION

1. Reckitt Benckiser Group plc (**RB**) is a global consumer goods company, headquartered in the UK. It has 106 brands, including the Durex brand. Durex's product range includes personal lubricants.

2. The K-Y brand and associated assets (the **K-Y brand**) are owned by McNeil-PPC Inc., a subsidiary of Johnson & Johnson (**J&J**) headquartered in New Jersey, USA. In the UK, J&J supplies only its basic 'K-Y Jelly' product.

3. On 19 December 2014, the Competition and Markets Authority (**CMA**) decided under section 33(1) of the Enterprise Act 2002 (the **Act**) that it is or may be the case that the anticipated acquisition by RB of the K-Y brand from McNeil-PPC, Inc, a subsidiary of J&J (the **Merger**) may be expected to result in a substantial lessening of competition (**SLC**) within a market or markets in the United Kingdom (the **SLC Decision**).

4. However, the CMA did not refer the Merger for a phase 2 investigation pursuant to section 33(3)(b) to allow the Parties the opportunity to offer undertakings to it for the purposes of section 73(2) of the Act within the five working day period under section 73A(1) of the Act.

5. On 30 December 2014, RB offered the CMA two alternative remedies (together the **Proposed Remedies**):

(a) A behavioural remedy which consisted of maintaining [✂] and quality of K-Y products currently sold in the UK by J&J for five years (the **Proposed Pricing Remedy**).

(b) A licensing remedy (the **Proposed Licensing Remedy**) consisting of RB entering into an exclusive license with a third party for a four-year period to allow the licensee to sell the K-Y products currently sold in the UK by J&J, followed by a one-year period during which RB would not be permitted to sell K-Y branded products in the UK (the **Blackout Period**). [✂].

ASSESSMENT OF THE UNDERTAKING

6. In the SLC Decision, the CMA decided that it is or may be the case that the Merger may be expected to result in an SLC in the market for the supply of personal lubricants to grocery retailers and national pharmacy chains in the UK.

7. The SLC Decision states that if, pursuant to section 73A(2) of the Act, the CMA decides there are no reasonable grounds for believing that it might accept any undertaking offered by the Parties, or a modified version of it, then the CMA will refer the Merger pursuant to sections 33(1) and 34ZA(2) of the Act.

8. The CMA has an obligation under the Act in the phase 1 stage of its review to have regard, when accepting undertakings in lieu, to the need to achieve as comprehensive a solution as is reasonable and practicable to the SLC and any adverse effects resulting from it (section 73(3) of the Act). Accordingly, the remedies proposed must be clear-cut and capable of ready implementation.[1] This means, amongst other things, that the CMA must be confident that all the potential competition concerns that have been identified in its investigation would be resolved by means of the undertakings in lieu without the need for further investigation.

Proposed Pricing Remedy

9. The CMA considers that the Proposed Pricing Remedy is not (i) sufficiently clear-cut, and (ii) not capable of fully addressing the competition concerns identified in the SLC Decision. As noted in the Exceptions Guidance, the CMA is unlikely to consider, at the first phase, that behavioural undertakings will be

[1] *Mergers – Exceptions to the duty to refer and undertakings in lieu of reference guidance* (OFT1122, December 2010 (***Exceptions* Guidance**), adopted by the CMA as set out in *Mergers: Guidance on the CMA's jurisdiction and procedure*, Annex D), at paragraphs 5.6-7.

sufficiently clear-cut to address the identified competition concerns. This is because behavioural remedies bring a number of risks which can reduce their effectiveness or create competition concerns elsewhere. These concerns relate to monitoring, enforceability and a number of other risks they may bring which can reduce their effectiveness or create competition concerns. [2]

10. Against the background of this general policy, the CMA has considered the Proposed Pricing Remedy's ability to offer a sufficiently clear-cut solution to the concerns it has identified. The CMA notes that the proposal [✂] may increase price transparency and, as such, may be capable of facilitating collusion or coordination. It also notes that the Proposed Pricing Remedy does not address a possible worsening of the offer insofar as it relates to (a reduction in) innovation or product development. In that respect, it does not fully address the competition concerns identified in the SLC Decision. The CMA also notes that any effective remedy would need to apply as long as an SLC persists to provide a clear-cut solution. It considers that this period is difficult to predict in this case as it is uncertain to what extent market conditions may evolve in the next five years. It is therefore not sufficiently clear that any remedy would no longer be required after this relatively short period.

11. The CMA therefore considers that the Proposed Pricing Remedy offered by RB is not a clear-cut solution to the competition concerns identified as arising from the Merger.

Proposed Licensing Remedy

12. The CMA considered whether the Proposed Licensing Remedy was sufficiently clear-cut and practicable to give the CMA confidence that the competition concerns identified in the SLC Decision would be fully addressed.

13. As noted in the Exceptions Guidance, in appropriate cases, the CMA may accept quasi-structural undertakings in lieu of reference such 'as to grant a divestment purchaser a perpetual and royalty-free licence'. [3]

14. In previous cases, where the Office of Fair Trading (OFT) accepted licensing remedies at phase 1, the Proposed Licensing Remedy involved an exclusive perpetual license.[4]

---

[2] See the Exceptions guidance regarding the risks raised by behavioural remedies, paragraphs 5.39-41.

[3] At paragraph 5.24.

[4] See the remedies accepted by the OFT regarding the acquisition of Unilever by Alberto Culver (2010) and regarding the anticipated acquisition by Tetra Laval of part of Carlisle Process Systems (2006).

15. The European Commission's notice on remedies states that 'In exceptional cases, the Commission has accepted commitments to grant an exclusive, time-limited licence for a brand with the purpose of allowing the licensee to re-brand the product in the period foreseen' and that 'both the licence and the Blackout Period have to be sufficiently long, account being taken of the particularities of the case, so that the re-branding remedy is in its effects similar to a divestiture'. [5]

16. However, in its Merger Remedies Study,[6] the European Commission noted that temporary licenses were liable to 'create uncomfortable brand splitting situations' and that a permanent license gives the buyer 'increased incentive and ability to compete' compared to a temporary license.

17. Having considered the Proposed Licensing Remedy, the CMA is not confident that the time-limit proposed by RB would give the potential licensee the necessary incentives and ability to compete sufficiently strongly with RB.

18. The CMA has significant doubts that the proposal is sufficient to allow the potential licensee to compete effectively in the short-term using the K-Y brand, and in the long term to develop a sufficiently strong brand with a level of consumer awareness and loyalty equivalent to the K-Y brand.

19. Furthermore, the CMA considers that the licensee of the Proposed Licensing Remedy, in view of the relatively short duration proposed, may have conflicting incentives: (i) to run down or not to invest in the K-Y brand in order to develop its own brand, which would reduce competition to RB in the short term; and (ii) to develop the K-Y brand at the expense of promoting its own brand and promoting competition with RB in the longer term. Given the uncertain resolution of these conflicting incentives, the CMA does not believe that the competition concerns identified in the SLC Decision would be fully addressed by the Proposed Licensing Remedy.

20. Finally, the CMA is not certain that the competition concerns identified in the SLC Decision would not persist beyond the period of the Proposed Licensing Remedy.

21. In addition to its duration, other aspects of the design and scope of the Proposed Licensing Remedy raise questions regarding its ability to address competition concerns identified in the SLC Decision in a clear-cut manner:

---

[5] Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004, paragraphs 39-42.

[6] Merger Remedies Study, DG COMP, European Commission, October 2005.

(a) [✂].

(b) The general limitation on the potential licensee doing anything that could devalue or damage the K-Y brand may both: (i) prevent the potential licensee from co-branding the K-Y product with its own product during the exclusive licensing period and (ii) limit its ability to develop its branded product separate from K-Y before the Blackout Period.

(c) The Proposed Licensing Remedy does not ensure that the potential licensee would replace J&J in its relations with grocery retailers and national pharmacy chains. Grocery retailers may simply resume relations with RB regarding the K-Y brand at the end of the Blackout Period.

(d) In the absence of a firm offer of an upfront buyer and of a monitoring trustee from the beginning of the implementation of the Proposed Licensing Remedy, there are increased risks regarding the enforcement and monitoring of the Proposed Licensing Remedy.

22. However, even if RB's offer was modified to address the CMA's concerns described in the paragraph above, the limited duration of the Proposed Licensing Remedy, as explained above, would not make it sufficiently clear-cut to address the competition concerns identified in the SLC Decision.

23. The CMA therefore considers that the Proposed Licensing Remedy offered by the parties is not a clear-cut solution to the competition concerns identified as arising from the Merger in the SLC Decision.

DECISION

24. After examination of the Proposed Remedies, the CMA does not believe that they would achieve as comprehensive a solution as is reasonable and practicable to the SLC identified in the SLC Decision and the adverse effects resulting from that SLC.

25. Accordingly, the CMA has decided not to exercise its discretion under section 73(2) of the Act to accept undertakings in lieu of reference.

26. The Merger will **therefore be referred** pursuant to sections 33(1) and 34ZA(2) of the Act.

Sheldon Mills
Senior Director of Mergers
Competition and Markets Authority
7 January 2015