The Competition Appeal Tribunal: a new venue for challenging restrictive covenants?

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Restrictive covenants are a common feature of business sale and property transfer agreements. In many cases, these will not restrict competition. However, in some circumstances, they may do so and be at risk of challenge by the party bound by the covenant, seeking its release from the covenant and, potentially, damages for losses suffered by it.

In a recent case brought in the Competition Appeal Tribunal (CAT), *Shahid Latif v Tesco*,[1] the claimants challenged a restrictive covenant contained in a property transfer agreement. Although this settled at an early stage, it demonstrates that the CAT (and not the High Court) may be an appropriate venue for challenging anti-competitive covenants contained in business sale or property transfer agreements that infringe the Competition Act 1998 (CA 1998).

The claimants in *Shahid Latif v Tesco* availed of a new procedure, known as the "fast-track" procedure, which enables claims under the CA 1998 to be brought quickly and at low cost, in particular by individuals, micro-businesses and small and medium-sized enterprises (SMEs). This may well be a suitable procedure for claims brought by SMEs to be released from restrictive covenants that limit their ability to compete.

Restrictive covenants in business sale and land agreements

When a business is sold or ownership of property is transferred, it is common for the vendor to be subject to a restrictive covenant.

A business vendor may be restricted from competing with the business sold by it for a particular period, whilst the vendor or transferor of land may be restricted from using or disposing of any retained property for specific purposes. Such covenants are intended to protect the value of the goodwill or property acquired by the purchaser. It is equally possible, although less common, that the purchaser may agree not to compete with the vendor's retained business.

Similarly, covenants in commercial property leases may restrict either the landlord (in respect of retained premises) or the tenant (in respect of the demised premises) in the use to which the relevant premises may be put. The landlord may be prevented from leasing the retained premises (for example, other units in a shopping centre) to companies that compete with the tenant. Alternatively, the tenant may be restricted in the goods or services it can sell from the demised premises.

Application of the Chapter I prohibition to restrictive covenants

The CA 1998 prohibits anti-competitive agreements and concerted practices (the Chapter I prohibition: s.2) and the abuse of a dominant position (the Chapter II prohibition: s.18). A restrictive covenant is an agreement for the purposes of s.2 of the CA 1998. Where a dominant undertaking imposes a covenant upon another undertaking, this may potentially constitute abusive behaviour for the purposes of s.18.

Many such covenants will not restrict competition, whether by object or effect, although in some circumstances they may do so. Much will turn on the facts of the individual case.

In general, in business sale agreements, a non-compete covenant accepted by the vendor that is in excess of three years' duration (or which is broader in product and/or geographic scope than that of the business being sold) will generally be considered not to be "ancillary" to the transaction and will likely restrict competition.[2] In *Areva* and *Siemens* (which concerned covenants applying after termination of a joint venture), the Commission considered that a non-compete restraint on Siemens (the exiting party) was lawful only for three years and only for the products manufactured by the joint venture.[3] It also considered that restraints of unlimited duration not to disclose the technological know-how and confidential information of the joint venture did not restrict competition, although obligations not to use such know-how or information did so, so were enforceable for only three years as "ancillary restraints".

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[1] Case No.1247/5/7/16 *Shahid Latif and Mohammed Abdul Waheed v Tesco Stores Ltd*. A summary of the Claim, published by the CAT, is available at: *http://www.catribunal.org.uk/files/1247_Latif_Summary_180216.pdf* [Accessed 1 August 2016].

[2] See Commission Notice on restrictions directly related and necessary to concentrations [2005] OJ C56/24 ("Ancillary Restraints Notice"), thus paras 10–26. It should be noted that where goodwill is not transferred, a non-compete obligation should not exceed two years in order to be considered as "ancillary" and falling outside of art.101 TFEU and the Ch.I prohibition.

[3] Case 39.736 *Areva* and *Siemens* [2012] OJ C280/8. The parties had, when establishing their joint venture, agreed on a post-termination restraint of 11 years that would extend to certain related products manufactured by Areva. The Commission considered that this was of excessive duration and scope, so was not an "ancillary restraint" and did not meet the requirements for exemption under art.101(3) TFEU.

In the context of a business sale, a non-compete covenant accepted by a purchaser is generally considered to restrict competition; it does not have any objective justification and is likely be regarded as a "hard core" illegal market-sharing agreement.[4]

In the context of real property transactions, a covenant contained in a transfer agreement or a lease will generally not be restrictive of competition "by object",[5] but may restrict competition "by effect" if it has, actually or potentially, an appreciable negative effect on competition.[6] Such effects may be due to the agreement excluding ("foreclosing") competitors from the relevant market (for example grocery retailing in a town), whether individually or cumulatively with other similar agreements. It will also be necessary to show that such agreements do not have countervailing benefits for consumers and thus does not benefit from an exemption; in *Martin v Crawley BC* (where a negative effect on competition was conceded by the defendant landlord), it was held that restrictions on the goods a tenant could sell from the demised premises did not satisfy the requirements for an exemption under s.9 of the CA 1998.[7]

The CAT's jurisdiction and the "fast-track" procedure

The CAT is an independent specialist statutory[8] competition law tribunal that hears and decides a range of competition and regulatory cases,[9] including claims for damages for losses caused by infringements of ss.2 and/or 18 of the Act and equivalent provisions of EU competition law, pursuant to s.47A of the CA 1998.

In 2015, the Consumer Rights Act (CRA 2015) extended the CAT's jurisdiction in a number of respects, including to hear both "follow-on" claims for damages (i.e. after the Competition and Markets Authority (CMA) or European Commission has adopted a decision that UK or EU competition law[10] has been infringed) and "standalone" actions (where no such decision has been adopted and the claimant must thus prove that an infringement has been committed).[11] Such claims may be claims for damages, any other sum of money or an injunction.[12]

A new procedure, the "fast-track" procedure, was also introduced as part of the 2015 reforms.[13] In particular, this procedure is intended to make it easier for individuals, micro-businesses and SMEs to obtain redress for harm suffered by anti-competitive behaviour, although its use is not restricted to such claimants.[14] However, the fact that a claimant is an SME does not in itself bring a claim within the "fast-track" procedure: in designating a case to be subject to the procedure, the CAT must have regard to all relevant considerations (including those set out in r.58(3)) in deciding that a case is suitable for the procedure.[15] There can be no presumption that a case should be allocated to the procedure.[16]

Claimants may apply to the CAT for an order that the claim be subject to the "fast-track" procedure; the CAT may also make such an order on its own initiative.[17] For claimants, an advantage of the procedure, in addition to its speed, is that the defendant's recoverable costs are to be capped at a level to be determined by the CAT.[18]

This reduces claimants' costs exposure, should they be unsuccessful. The cap will be determined by the CAT on a case-by-case basis, in order to give effect to the general principle that the court should allow only costs which are proportionate to the matters in issue[19] and, more specifically under the "fast-track" procedure, that this strikes a fair balance between the claimant's access to justice and the defendant's interest in not having to defend a claim that is unfounded; thus the cap may be lower than costs which are proportionate.[20]

[4] Ancillary Restraints Notice, para.17. See also Case 39.830 *Telefónica and Portugal Telecom* [2013] OJ C140/11, in which the Commission imposed fines of over €79 million on Telefónica and Portugal Telecom for agreeing, when terminating a joint venture in Brazil, not to compete with each other in the Iberian telecoms market, other than through their existing activities, from 27 September 2010 until 31 December 2011. The General Court upheld the Commission's decision that this constituted a "by object" restriction of competition and was not ancillary to the termination of the joint venture, although it held that the Commission had incorrectly calculated the fines imposed by it: *Portugal Telecom v Commission* (T-208/13) EU:T:2016:368 and *Telefónica v Commission* (T-216/13) EU:T:2016:369.

[5] *SIA "Maxima Latvija" v Konkurences padome* (C-345/14) EU:C:2015:784; [2016] 4 C.M.L.R. 1 at [21]-[24]. This is considered in more detail in O'Regan, *European Court of Justice provides guidance on when provisions of property leases may be anti-competitive* (2 December 2015), *http://www.stjohnschambers.co.uk/dashboard/wp-content/uploads/Property-leases-and-competitive-law.pdf* [Accessed 1 August 2016].

[6] *SIA "Maxima Latvija"* [2016] 4 C.M.L.R. 1 at [26]–[29]. See generally OFT Guidance, *Land Agreements: The Application of competition law following the revocation of the Land Agreements Exclusion Order* (OFT1280a, March 2011).

[7] *Martin Retail Group Ltd v Crawley BC* [2014] L. & T.R. 17; [2014] 1 E.G.L.R. 42. See O'Regan, *European Court of Justice provides guidance on when provisions of property leases may be anti-competitive* (2 December 2015), for commentary.

[8] Enterprise Act 2002 (EA 2002) s.12(1) and Sch.2.

[9] See generally CAT Guide to Proceedings 2015, ss.1 and 2, *http://www.catribunal.org.uk/files/Guide_to_proceedings_2015.pdf* [Accessed 1 August 2016].

[10] i.e. the Chapter I and Chapter II prohibitions of the CA 1998 or arts 101(1) or 102 TFEU.

[11] CA 1998 s.47A(2), inserted by Sch.8 para.4 to the CRA 2015.

[12] CA 1998 s.47A(3). Claims for injunctions may be brought only in England and Wales or Northern Ireland: s.47A(3)(c). In Scotland, a claim for an interdict cannot be brought in the CAT and must be brought in the Court of Session.

[13] EA 2002 Sch.4 para.15A, inserted by CRA 2015 Sch.8 Pt 2 para.31: this enabled the CAT to lay down rules for a "fast-track" procedure. The CAT did so by adopting The Competition Appeal Tribunal Rules 2015 (SI 2015/1648) (CAT Rules 2015), which came into force on 1 October 2015 and apply to claims brought thereafter.

[14] See CAT Rules 2015 r.58(3)(a) and CAT Guide to Proceedings 2015, para.5.140.

[15] *Breasley Pillows Ltd v Vita Cellular Foams (UK) Ltd* [2016] CAT 8 at [14]. See also CAT Guide to Proceedings, paras 5.145–5.146.

[16] *Breasley* [2016] CAT 8 at [29].

[17] CAT Rules 2015 r.58(1) and CAT Guide to Proceedings 2015, para.5.142. Where the CAT declines to order a case to be subject to the "fast-track" procedure, the CAT may nevertheless expedite the hearing if the case is urgent: CAT Guide to Proceedings 2015, para.5.141.

[18] CAT Rules 2015 r.58(2)(b).

[19] See Civil Procedure Rules r.44.3 and 44.4. Thus, on the "standard basis" of assessment, a successful defendant could recover from the other party the lowest amount which it could reasonably have been expected to spend in order to have is case conducted and presented proficiently, having regard to all the relevant circumstances: *Kazakhstan Kazagy Plc v Zhunus* [2015] EWHC 404 (Comm); 158 Con. L.R. 253 at [13].

[20] *Socrates Training Ltd v The Law Society of England and Wales (Costs Capping)* [2016] CAT 10 at [14]. Thus, in a claim valued at up to £500,000, the defendant's recoverable costs were capped at £350,000, even though it had prepared a costs budget of over £600,000. It should, however, be noted that the CAT did not criticise the defendant for choosing to instruct City of London solicitors instead of a less expensive regional firm in Birmingham. The CAT also capped the claimant's recoverable legal costs at £200,000, instead of its budgeted £220,000.

A claimant may also apply for an interim injunction, without being required to give a cross-undertaking in damages or with the amount of any such cross-undertaking being capped.[21] As the "fast-track" procedure is well suited to applications for injunctions, this is likely to be an important factor in favour of SME's use of it, although there can be no certainty that the CAT will order that no cross-undertaking is required, given its effect on defendants in cases where it is later shown that no injunction should have been granted in the first place. However, this may also increase the incentives for defendants to settle some cases.

For a claim to be allocated to the "fast-track" procedure, a final substantive hearing must generally be fixed to commence within six months of the CAT's designation order.[22] In addition, this hearing should ordinarily be for no more than three days.[23] Although this is not an absolute limit, cases of longer duration are unlikely to be suitable for the "fast-track" procedure.[24]

The "fast-track" procedure is particularly suitable for claims that are neither legally or factually complex nor raise novel issues[25] and will not require interlocutory hearings on points of principle. Such claims will have limited evidential requirements (including as to documentary evidence, witness of fact and expert witnesses) and will generally not require extensive disclosure of documents.[26] The "fast-track" is also likely to be suitable for claims in which no, or only limited, claims for damages are made.[27] It may therefore be well suited to claims where injunctive relief is sought.[28]

"Fast-track" cases will generally not require extensive disclosure,[29] and any disclosure will be tightly managed by the CAT, which may limit disclosure to specific disclosure.[30] In *Breasley* (a follow-on cartel damages claim) the claimants sought extensive disclosure from the defendants in order to quantify their claim for damages: the CAT considered that such disclosure was "of a scale and scope that is well beyond what is commensurate with the ['fast-track' procedure]".[31] The procedure is more likely to be appropriate where witness evidence (including expert evidence)[32] is limited in number and scope and documentary evidence is limited to documents attached to witness statements.[33]

Shahid Latif v Tesco: facts and outcome

In 1997, the claimants sold land in the small Derbyshire town of Whaley Bridge[34] to Tesco, the largest supermarket retailer in the UK. Tesco subsequently built a supermarket on the land acquired by it. The claimants retained adjacent land and covenanted with Tesco that they would not "use or permit the retained land to be used for the sale of food convenience goods or pharmacy products".[35]

In 2015, the claimants intended to sell the retained land to B&M Bargains, a discount retailer, but they first needed to be released from the covenant by Tesco. Perhaps not unsurprisingly, Tesco refused to do so.[36]

On 5 February 2016, the claimants brought proceedings in the CAT, alleging that the covenant restricted competition (presumably in the sale of groceries, convenience goods and/or pharmacy products) in the relevant geographic area (presumably the Whaley Bridge area), thereby infringing the Chapters I and/or II prohibitions. It was further alleged that the covenant was an unlawful restraint of trade contrary to the common law doctrine of restraint of trade. The claimants sought declaratory and injunctive relief as well as damages, including exemplary damages.[37] They applied for the claim to be allocated to the "fast-track" procedure.

[21] EA 2002 Sch.4 para.15A(3), inserted by Sch.8 Pt 2 para.31 to the CRA 2015. In deciding whether to require the claimant to provide a cross-undertaking in damages or to cap any such undertaking, the CAT will consider if this is necessary or appropriate in the interests of justice, taking account of the strength of the claimant's case, any loss that the respondent might suffer if an interim injunction is incorrectly granted and the claimant's financial resources: CAT Guide to Proceedings 2015, para.5.147.
[22] CAT Rules 2015 r.58(2)(a). In practice, allowing for around one month for an application for the claim to be allocated to the "fast-track" at the first case management conference, this would mean the main substantive hearing being held within around seven months from a claim being issued.
[23] CAT Rules 2015 r.58(3). This does not, however, mean that where it is estimated that substantive hearing will last for more than three days, the CAT cannot order a claim to be subject to the "fast-track" procedure. However, in such cases it is less likely that the CAT will designate a case as being subject to that procedure.
[24] *Breasley* [2016] CAT 8 at [19]. It should also be noted that the three day duration is for the entire trial.
[25] CAT Rules 2015 r.58(3)(c). This does not, however, mean that more complex cases cannot be brought using the "fast-track" procedure. In *Socrates* (a claim alleging that the Law Society has abused a dominant position by refusing to accredit the claimant's training courses), the CAT has ordered a split trial, with liability (and the availability of an injunction to restrain any infringement of the Chapter II prohibition) to be determined in the first trial (to be conducted under the "fast-track" procedure) and the questions of causation of loss and quantification of damages to be heard after judgment on liability, if required: see CAT Order of 16 May 2016, *http://www.catribunal.org.uk/files/1249_Socrates_Order_180516.pdf* [Accessed 1 August 2016].
[26] See CAT Rules 2015 r.58(3)(g).
[27] See CAT Rules 2015 r.58(3)(h).
In ordinary CAT proceedings, a party will be required to prepare a "disclosure report", listing all relevant documents held by it, including electronic documents, in respect of which an "electronic documents questionnaire" shall be completed: CAT Rules 2015 r.60. The CAT will then make orders as to the disclosure required to be given and how it shall be given: r.60(2) and (3).
[28] *Breasley* [2016] CAT 8 at [30] and [31]. Thus, claims for damages are unlikely to be suitable for the "fast-track" procedure, although, if damages are sought, it may be appropriate for a "split" hearing to be ordered, with the first trial being allocated to the "fast-track" procedure, but being limited to questions of liability, i.e. whether the restrictive covenant infringes the Ch.I prohibition, and whether an injunction should be granted. Questions of damages (i.e. causation and quantification of loss) would, if required, be determined in a second subsequent trial. The CAT applied this approach in *Socrates*.
[29] See CAT Rules 2015, r.58(3)(g).
[30] CAT Guide to Proceedings 2015, para.5.148.
[31] *Breasley* [2016] CAT 8 at [27].
[32] *Breasley* [2016] CAT 8 at [30]. The procedure may be appropriate if expert evidence is limited: ibid., referring to *Socrates*, in which expert evidence was confined to issues of market definition and dominance.
[33] *Breasley* [2016] CAT 8 at [22].
[34] Whaley Bridge is a town of approximately 6,500 people in the High Peak District, some 26km south of Manchester and 11km north of Buxton.
[35] *Shahid Latif v Tesco*, Summary of Claim.
[36] Press reports suggest that Tesco had initially agreed to release the covenant, in return for a payment by the developers, but then refused to complete the transaction. See, for example, *http://www.retailagency.co.uk/tesco-sued-for-breaching-competition-law/* [Accessed 1 August 2016].
[37] The CAT does not have jurisdiction to grant declaratory relief, this not being within the scope of claims set out in s.47A(3) of the Act. Furthermore, as a statutory tribunal, it does not have jurisdiction to hear claims based upon the common law doctrine of restraint of trade. To pursue such claims, a claim would need to be brought in or transferred to the High Court pursuant to the CAT Rules 2015 r.71.

On 17 March 2016, four days before the first case management conference (and thus before any procedural steps had been undertaken), it was announced that Tesco had released the claimants from the covenant. Accordingly, the claim was withdrawn, without Tesco having served its defence and with no costs order being made.[38]

Conclusion

By bring proceedings that they intended would use the CAT's "fast-track" procedure, the claimants in *Shahid Latif v Tesco* were able to achieve through litigation, and quickly and (presumably) at low cost, their commercial objectives when negotiations had failed.

An early settlement was also achieved in one of the three other "fast-track" cases brought so far, *NCQR v Institution for Occupational Safety and Health*, in which the defendant settled a claim alleging a breach of the Chapter II prohibition by granting accreditation for the claimant's diploma qualification.[39]

Whether a restrictive covenant is anti-competitive will depend on the facts of the individual case, in particular the extent to which it does or may restrict competition in the relevant product and geographic markets. In the case of a property covenant, this is likely to be a local market. These claims are unlikely to be factually or legally complex and the principal objective of such claims will often be to obtain release from the covenant (whether through settlement, as in *Shahid Latif*, or judgment) and not to obtain damages. They will ordinarily not require extensive factual or expert witness evidence or be "document heavy" cases.

The CMA is unlikely, as a matter of administrative priority, to investigate complaints concerning a single covenant and affecting only a local market. High Court proceedings may be lengthy and expensive. As an alternative, and whilst there can be no certainty that the CAT will grant an application for a claim to be allocated to the "fast-track", this being at the CAT's discretion, the CAT's "fast-track" procedure may be well suited to challenging the validity of restrictive covenants. It is a quick and relatively cheap means, particularly for individuals and SMEs, of dealing with such cases, with limited exposure to costs orders in the event of a claim being unsuccessful. Indeed, a defendant's limited ability to recover its costs of a successful defence may well be a factor in reaching settlement on commercial grounds.

Individuals and companies that are subject to restrictive covenants, whether given in the context of a business sale or a property sale or lease, may therefore wish to consider if there are grounds to challenge them before the CAT. However, for their claim to be suitable for the "fast-track" procedure, care must be taken to ensure that the requirements of r.58(3) of the CAT Rules 2015 are satisfied, in particular as to the duration of the final hearing, the evidence that is required and limits on disclosure.

[38] *Shahid Latif v Tesco*, CAT Order of 17 March 2016, *http://www.catribunal.org.uk/files/1247_Latif_Order_170316.pdf* [Accessed 1 August 2016].
[39] *NCQR Ltd v Institution for Occupational Safety and Health*, Case Nos 1242/5/7/15(IN) and 1242/5/7/15, CAT Order of 11 January 2016, *http://www.catribunal.org.uk/files/1242-1243_NCRQ_Order_120116.pdf* [Accessed 1 August 2016].