

Mr Patrick Gerard

Your ref
Our ref CE/6001/05
Date 26 April 2005

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Dear Mr Gerard,

Thank you for your letter of 9 April and the enclosed submission to Sir John Vickers, Chairman of the Office of Fair Trading (OFT), about the use of comparative pay positioning for setting levels of pay for company executive directors. You ask the OFT to investigate the issue that you have raised as a matter of priority. The Chairman has asked me to reply to your letter on his behalf.

You raise a number of interesting points in your submission about the nature of competition in this area, and I know this is probably an overly simplistic summary of your argument, conclude that the Combined Code of Corporate Guidance has not addressed the issue of executive pay as was its intention and created an upward ratchet effect on levels of executive pay (through the creation of remuneration committees and consultancies).

As you know, the Chapter I prohibition prohibits agreements between undertakings, decisions by associations of undertakings or concerted practices which may affect trade within the UK and have as their object or effect the prevention, restriction or distortion of competition within the UK.

In order for the OFT to conduct an investigation it must first satisfy itself that there are reasonable grounds for suspecting an infringement of the Competition Act 1998 (the Act). Reasonable grounds must be based on fact and be capable of being substantiated. In this regard you do not, aside from some isolated and mainly anecdotal references, provide any actual data or analysis in relation to executive pay levels in the UK. It is not possible, therefore, to see whether there is any commonality of prices or terms and conditions in relation to Executive pay levels. Further, *if* there were commonality or similarity in the terms and conditions between firms recruiting executive directors we would then have to satisfy ourselves that there was some evidence to suggest that the commonality was a result of agreement (or of a concerted practice) between undertakings.

To be clear, it is not an infringement of the Act for an undertaking to consider what comparable Executive remuneration levels and packages are on offer when considering what terms and conditions it might offer to attract candidates to an executive position in its firm. Indeed, this sort of price bench-marking exercise is common in most markets and does not necessarily adversely impact on competition (i.e. Pepsi look at Coca Cola prices when pricing, Cadbury look at Nestle's

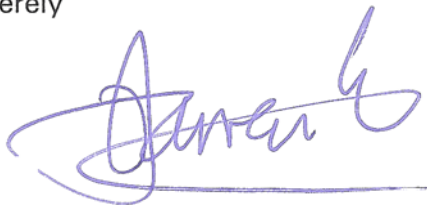


confectionary prices, etc.) and - provided the competitive process is not impeded - this normally results in a downward pressure on prices. If prices go up this may be because there is a scarcity in supply or reflect the premium nature of the product or service being supplied. Price levels should be able to move up as well as down in a functioning competitive market. This is one of the reasons why the OFT is not a price regulator because price regulation can distort the proper operation of markets.

As a general comment on the information supplied, your complaint does not specifically identify who the parties, or likely parties, to the agreement or concerted practice might be or any verifiable evidence to support your argument of contact between them. The OFT would also have to consider the question of market definition i.e. is the supply of executive directors, or any other plausible market definition that might be advanced, a relevant market for the purposes of the Act? This question is not addressed at all in the submission but it is something that the OFT would have to have regard to in assessing whether the alleged agreement (or concerted practice) might have an appreciable effect on competition in a relevant market.

While the OFT does not expect complainants to provide all the information that might be required to prove an infringement before it will investigate it does need to satisfy itself that the 'reasonable grounds for suspecting' criterion is met. Further, in considering whether a case is a priority for investigation the OFT will take into account the extent and nature of information readily available to the OFT, the prospect of gathering further evidence and the time and resources needed to do so. In conclusion, the OFT is not minded for these reasons to conduct an investigation into the matters you raise at this time.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Darren Eade', with a horizontal line underneath it.

Darren Eade
Competition Enforcement Division 5