

# Walpole

## **Consultation on the UK Retained Vertical Block Exemption Regulation ("VBER") Walpole British Luxury Submission**

**21st July 2021**

We refer to the consultation paper issued by the Competition and Markets Authority ("CMA") on 17 June entitled "The retained Vertical Agreements Block Exemption Regulation Consultation document". This letter sets out Walpole's response to the CMA's consultation document.

### **Walpole – who we are**

Walpole is the official sector body for UK luxury. Founded in 1992 as a not-for-profit organisation, it counts more than 250 British brands in its membership and is recognised in both Westminster and Brussels. As the voice of British luxury, Walpole's purpose is to promote, protect and develop a sector worth £48 billion to the UK economy and that is a leading creator of long-term sustainable employment and driver of tourism into the UK.

Walpole's 250 members are spread across all sub-sectors of the luxury industry (automotive, beauty & fragrance, fashion, food & drink, hospitality & services, jewellery, interiors, property and retailers) from small and medium-sized enterprises (SMEs) to internationally owned and publicly listed companies. Walpole promotes international business opportunities, driving growth in the sector through a programme of initiatives, including the annual trade mission and press showcase to the US. As founders of the European Cultural and Creative Industries Alliance (ECCIA), Walpole actively represents the views and interests of the UK luxury sector with Europe's luxury and creative sectors,

An important element in the continued success of our members is the ability to ensure that their goods are sold efficiently and appropriately. Maintaining the aura of luxury and prestige is a vital component in that endeavour. The ability to put in place appropriate controls through distribution and retail agreements is in turn key to achieving these goals. This consultation is therefore of great importance to Walpole's members.

Our responses follow. We have answered below those of the CMA's questions which are of particular importance to our members.

## Walpole responses to CMA questions

### Policy and impact questions

**Question 1: Do you agree with the CMA's proposed recommendation to the Secretary of State to make a Block Exemption Order to replace the retained VABER with a new UK VABEO, rather than letting it lapse without replacement or renewing without varying the retained VABER?**

- a) Yes**
- b) No**
- c) Not sure**

**Question 2: Please explain your response providing, where possible, examples and evidence to support your answer.**

As the CMA has identified in its consultation paper, it is vital for businesses to have the legal certainty of the safe harbour. That enables businesses to structure their distribution arrangements with confidence. Self-assessment without a safe harbour is not a satisfactory substitute, however good the guidelines which are provided. Self-assessment without a safe harbour regulation does not provide the same degree of reassurance and would give scope to an increased level of litigation to resolve whether or not a distribution agreement was compliant. The key difference is that a block exemption lays down a number of objectively determinable criteria enabling business to arrive at a conclusion as to whether or not the agreement is compliant.

**Question 3: How will the proposed UK VABEO as outlined in the CMA's proposed recommendation impact consumers?**

- a) Significant positive impact**
- b) Moderate positive impact**
- c) Negligible impact**
- d) Moderate negative impact**
- e) Significant negative impact**

### Policy questions

**Question 9: What are your views on the CMA's proposed recommendation on dual distribution?**

We consider the CMA is right to maintain the exemption for dual distribution. Walpole members have already provided reasons as to why this is essential for their commercialisation strategies. It is vital for them to maintain a network of independent online and retail outlets while also having their own vertically integrated shops.

**Question 10: Do you think that additional guidance on information exchange in the context of dual distribution would be helpful? If so, please provide your views on what that guidance should say.**

In our experience, we do not consider that further guidance in this area is necessary. The information exchange between manufacturers and retailers / distributors is generally benign and even pro-competitive.

One of our members provided evidence that the sort of information it would wish to obtain from independent retailers would relate to information about its own products, which ones were selling

well and sometimes in relation to customer guarantee schemes. It is difficult to see what prejudice to competition could be caused from this as there would be no competitive harm caused by the brand owner (as the operator of the monobrand channel) from simply knowing that a particular product was selling well in independent stores.

To lay down specific guidelines for this type of dialogue would risk disincentivising helpful interactions and sharing of ideas. Between suppliers and retailers. That could have a negative effect on consumer welfare because this discussion will frequently provide useful insights to both the manufacturer and the retailer which will assist them in optimising goods to consumer desires. For example, it can assist a manufacturer to know which of its new products is proving popular with customers.

If the CMA is inclined to issue guidance about illicit information sharing in the vertical context, that could focus on known antitrust problematic areas. For example, Amazon is currently under investigation for its alleged misuse of information about retailer sales to produce copycat goods. That, however, relates more to Amazon's position as a dominant provider of marketplace services. Likewise, the CMA could also remind parties of the risk of hub and spoke cartels where retailers become a conduit for sensitive information between rival suppliers at the manufacturing level.

### **Impact questions**

**Question 11: To what extent does the dual distribution exception for non-reciprocal vertical agreements, as outlined in the retained VABER, positively impact your business's operations or the operations of those you represent? Please explain your answer.**

- a) Completely**
- b) Very much**
- c) Moderately**
- d) A little**
- e) Not at all**

The principal benefit of a dual distribution system is a plurality of different types of sales outlet, which not only enhances consumer choice and allocative efficiency but also leads to innovation and creativity in the way that goods are sold. There is a degree of intrabrand competition which can be helpful but that is secondary to the consumer benefits of strong interbrand competition when brand owners are able to present their goods in ways that are optimal and enhance the value of their brands.

Other members have pointed to the benefits of having monobrand sales outlets through which they can obtain useful consumer feedback on new products. One of our members outlined how monobrand stores were important to its need to maintain luxury aura. That business has realised that brands need to get closer to the consumer in order to drive that prestige and "tell the story" of specific luxury goods. The monobrand stores are flagships, built to "bring the end customer into the universe". Many monobrand stores are also event locations where product launches take place and specific brands can be promoted.

Independent resellers may be more reluctant to stock experimental or slower moving goods which may be unpopular with customers. On the other hand, if sales through the monobrand stores have proved successful, independent retailers are more likely to sell those. It may not always be practical to require resellers to stock the full range of products.

Independent stores, however, perform a distinct but no less necessary role. For example, they enable the brand owner to achieve a higher degree of geographical coverage than would be the case if they

only sold through vertically integrated and directly owned stores. That improved distribution obviously provides pro-consumer benefits and enhanced consumer choice in provincial centres of population. Forcing brands to vertically integrate would be bad from the perspective of the brands (who generally do not wish to take this step) and could also potentially lead to job losses if independent retailers are forced to close because brands no longer sell their goods there.

One of our members commented that in the context of fashion items consumers may occasionally wish to have a multibrand experience, for example, where they will try on garments that have been manufactured by different brands together and compare and contrast the two. That risks being lost if the dual distribution exception is removed.

**Question 12: To what extent does the dual distribution exception for non-reciprocal vertical agreements, as outlined in the retained VABER, negatively impact your business's operations or the operations of those you represent? Please explain your answer.**

- a) Completely
- b) Very much
- c) Moderately
- d) A little
- e) Not at all

Our members are not aware of any drawbacks to dual distribution.

We are, however, concerned that certain theories have been advanced that dual distribution may be harmful to competition. We do not consider that any of these theories of harm have been fully substantiated with empirical evidence. We are not aware of any EU Commission decisions which have shown the model to be problematic from the vantage point of competition law.

On the other hand, our members are convinced that there are substantial advantages to maintaining a distribution system maintaining both vertically integrated and independent resellers. Those benefits must outweigh any theoretical risk that this tried and tested model of getting to market may entail.

**Question 13: What would be the likely impact on your business's operations, or the operations of those you represent, if the dual distribution exception was not included in the UK VABEO at all? Please include examples and where possible, quantitative and/or qualitative evidence in your answer.**

First and foremost we would be concerned at the potential loss of those significant advantages we outlined in our response to Question 11.

From the perspective of the U.K. as a place to do business, we also believe such a change would be a retrograde step. Brand owners may be deterred from investing in the jurisdiction if this would require them to choose between either monobrand stores or independent retail outlets. In most cases, they would wish to have both channels as a means of getting to market.

We also have a concern that if the exception were to be ended, brand owners would be forced into an invidious position. They would be forced to choose between the vertically integrated stores and independent retail outlets.

Encouraging a move towards independent stores only would cost brand owners the ability to provide a forum where they could experiment with new goods and provide a sales outlet where the full range of goods were available. For our members as luxury brands, complete vertical integration is not a viable option although monobrand stores retain an important but distinct role in their whole getting to market strategy (see our response to Q.11).

On the other hand, if brand owners were to choose vertically integrated stores, that would increase the cost base, possibly leading to price increases for customers. This would also jeopardise independent retailers who may, as a consequence, find it more difficult to retain supplies of popular goods, thereby threatening their continued attractiveness for customers. The result could be job losses at independent retailers, who may be forced to curtail their activities due to an inability to source popular products from brands. This would not be a positive step for the UK economy nor address the current challenges faced by the High Street.

**Question 14: Do you consider the CMA's proposed recommendation, which also applies the exception to dual distribution by wholesalers and by importers, to have a positive or negative impact on business operations? Please explain your answer.**

- a) Significant positive impact**
- b) Moderate positive impact**
- c) Negligible impact**
- d) Moderate negative impact**
- e) Significant negative impact**

#### **Policy questions**

We have outlined above the positive effects of dual distribution for both brands and consumers. Extending such benefits to the wholesale channel would yield further benefits and provide flexibility.

Ending dual distribution would have a significant and adverse economic impact. Inevitably that would lead to brand owners using independent offline sellers less with an attendant loss of jobs with independent retailers. This would be most unhelpful at a time when retail has been severely impacted by Covid and the recovery is fragile.

**Question 15: Do you agree with the CMA's proposed recommendation on resale price maintenance (RPM)?**

We are broadly in agreement with the CMA's proposed approach. We would not propose that RPM should be re-cast from its current status as a hardcore restriction under the UK VABEO. We welcome the CMA's proposal to provide improved guidance in the accompanying guidelines for those exceptional circumstances where RPM may be permitted. As you know, our members (who are predominantly luxury brands or purveyors of luxury brands) have concerns that the exceptions are insufficiently clarified in the current vertical guidelines. As a result, Walpole members frequently have insufficient confidence to ever rely on RPM even where this may yield pro consumer efficiencies in the context of luxury goods and potentially be lawful.

From the perspective of luxury brands, it is important to appreciate that there is a connection between pricing and customer perception. It can be important for a brand owner wishing to preserve the positioning of their goods as luxury products to protect them from excessive discounting by resellers.

We will need to see of course the specific wording proposed in order to evaluate whether or not this addresses our current concerns. However, in principle, we are in favour of enhanced and improved guidance in this area.

**Question 16: Based on your experience, do you have any examples in practice of circumstances where RPM would lead to efficiencies that outweigh the restriction of competition? If so, please provide these examples**

Yes, in the context of luxury brands, this emanates from the fact that competition is based on quality and the aura of luxury rather than price. To that end, unrestrained discounting on products by resellers can be problematic as it runs counter to the idea that the products possess the aura of “luxury”.

Luxury means scarcity and there is often a balance between trying to sell as much as you can without impacting the prestige or aura. The quantity depends upon the goods, the product category but the element of scarcity is an essential part of the story. When you have a product discount of say 30% it undercuts the story the brand is trying to sell.

For example, we have set out below evidence that a brand may experience a situation where the lead designer of a line of luxury fashion items either leaves the brand or is replaced. One of our members provided evidence that where a designer change occurs, current customers will become temporarily alienated until they adapt to the new designer’s products. Shortly after the launch, it is important to ensure the new designs are not subject to excessive discounting as that may detract from their status as luxury items and suggest they have a different market positioning to their predecessors.

For seasonal ranges, the brand owner has a short time within which to sell the goods in which time you can tell the end customer what the product is about without being impacted by the possibility of discounting. Discounting by independent retailers can force a price war which the vertically integrated stores cannot themselves avoid. That would jeopardise the revenues of the manufacturer and detract from the aura of luxury which the brand wishes to convey. In such circumstances RPM would be very useful in order to allow the end customer to experience the brand and for the brand to have the longevity required.

**Question 17: Do you think that additional guidance on when RPM may lead to efficiencies would be helpful? If so, please provide your views on what that guidance should say.**

Walpole members have indicated that for the luxury sector improved guidance would be welcome in the following specific areas:

- With regard to product launches for luxury goods, it is legitimate that this continues to be recognised as an exceptional situation. That is particularly the case where the launch of new luxury products tests the positioning of the product as a luxury product; discounting of the same product by independent resellers in these circumstances can jeopardise that exercise as it diminishes the perception of prestige in the goods. Walpole members would appreciate more guidance as to how long would be considered a reasonable period for RPM to subsist in order to support the product launch, particularly in the context of luxury goods (in relation to which price competition is less important as a differentiating factor between comparable products);
- RPM may be justified for seasonal luxury products, which require substantial upfront investment (e.g. to launch and promote) but have a short lifespan on the shelves. If these products were substantially discounted, it would also put a strong downward pressure on prices charged both by independent resellers and by the brand direct from its own outlets

which would be forced to follow suit. In those circumstances, RPM may be needed in order to recoup the substantial investment and to protect their positioning as luxury products

- We would propose a further more general set of guidelines to recognise those situations where a brand owner may need to use RPM in order to preserve the aura of luxury in relation to a specific product (citing the given example below of a fashion line where there is a change of designer). There may be circumstances where a brand is subject to short term challenges or changes in circumstance with part of its product line where RPM may be needed to preserve the perception of the affected products as possessing a quality of luxury. An example would be where the designer of a line of fashion items changes. Preserving continuity with the previous products under the predecessor designer would require ensuring that the price of those products is not radically cut at retail level, or consumers may be deterred by what they perceive to be a new and less prestigious line. The value of the brand may be significantly harmed as a result.

### **Impact questions**

**Question 18: What would be the likely impact on your business, or those you represent, if RPM were not treated as a hardcore restriction for the purposes of the proposed UK VABEO? Please explain your answer.**

- a) **Significant positive impact**
- b) **Moderate positive impact**
- c) **Negligible impact**
- d) **Moderate negative impact**
- e) **Significant negative impact**

Our answer takes into account the position of luxury sectors.

In that context, Walpole members think that the loss of intrabrand competition from allowing the imposition of RPM should be balanced against the gains made from allowing optimal pricing of goods in a way that would promote the brand. In the context of luxury goods, excessive discounting can be a problem, particularly in the circumstances highlighted in our answers to Q16 and Q17.

The creation of the aura of luxury and prestige is damaged where consumers see price reductions because it suggests that the goods are unwanted and/or of inferior quality. It also runs counter to the creation of the impression that the goods are scarce, itself an important element in creating the impression that the goods possess a luxury quality.

In conclusion, in our view enabling luxury brands to position their products optimally would in our view enhance competition between similar owners and more than offset (to a small degree) the loss of intrabrand price competition between independent resellers of luxury goods.

**Question 19: Are you aware of, or have you encountered, any difficulties in your business as a result of the treatment of RPM as a hardcore restriction for the purposes of the retained VABER? If so, please give examples.**

### **Policy questions**

Yes, we refer you to the examples given in response to Question 16 above.

**Question 20: What are your views on the CMA’s proposed recommendation on territorial and customer restrictions? In particular, what are your views on the CMA’s proposed recommendation to:**

- a) continue to treat territorial and customer restrictions as ‘hardcore’ restrictions so as to remove the benefit of the block exemption (subject to exceptions);**
- b) maintain a distinction between active and passive sales;**
- c) revisit the distinction between active and passive sales for certain types of online sales in the CMA VABEO Guidance; and**
- d) change the current regime in order to give businesses more flexibility to design their distribution systems according to their needs?**

**In your response please consider whether:**

- a) there are any features of the UK internal market militating in favour or against retaining the treatment of territorial restrictions as ‘hardcore’ restrictions for the purposes of the UK VABEO;**
- b) the distinction between active and passive sales remains valid and whether changes to this categorisation should be made in order to:
  - i. clarify the situations where online sales amount to passive or active sales; or**
  - ii. give businesses more flexibility to combine different distribution models.****

We are broadly happy with the CMA’s proposals, which we consider represents a balanced approach.

With regard to point (a), the CMA should confirm it may be permissible to restrain active or passive sales of goods where that is required to ensure goods are sold in accordance with local marketing or other trading regulations.

We have addressed point (b) in more detail in response to Q21 below. We consider further guidance should be provided around when an online sale is truly passive. We do not consider it helpful or appropriate to continue with the presumption that all online sales are passive and this restricts brand owners from designing appropriate distribution systems which are responsive to the needs of their products.

Assuming the wording of Article 4 of the retained VBER is replicated in the UK VABEO, we would like to see an amendment to the wording of Article 4(b)(iii) of the VBER, which permits “the restriction of sales by the members of a selective distribution system to unauthorised distributors within the territory reserved by the supplier to operate that system”. The amended text should state “within the territory or territories reserved by the supplier to operate that system”. That would recognise that a selective distribution system may span a number of jurisdictions. It would also create harmony with Article 4(d) which forbids the reseller from restricting cross-supplies within the selective distribution system without reference to territories.

With regard to (c) we would recommend, that the use by a distributor of country specific adwords in search engine or certain online platforms with regional biases (e.g. Facebook groups with specific geographical orientations) marketing may evidence active selling.

We would also like to see in the new guidance a recognition that brand owners are able to prevent resellers from selling luxury goods on online platforms. The principles of the *Coty* judgment should be codified in the new guidance.

We would like to see within the new guidance the inclusion of a possibility for luxury brand owners to restrain the use of price comparison websites by distributors. Price competition is less important for luxury goods and the positioning of goods on such sites will frequently damage the image of the goods



in terms of being based on scarcity of supply and possessing a quality of luxury. As a more general point, brand owners should have the ability in any event to restrain the use of price comparison websites where that result in misleading or damaging marketing.

Finally, we would wish for the new guidance to cover the circumstances in which a brand owner may take steps to restrain grey market sales (discussed further in the following answer).

With regard to point (d), we consider such added flexibility is helpful. We have added some additional thoughts on this in response to Q21 below.

**Question 21: Do you agree that additional guidance on this issue would be helpful? If so, please provide your views on what that guidance should say including examples of situations where online sales should be regarded as passive or active sales.**

### **Impact questions**

We think it would be useful to provide more guidance in relation to permissible actions to restrain grey market sales. The general prohibition on passive and active sales can create difficulties for brand owners in restraining these.

Grey market sales are the ultimate form of free riding, damaging everyone in the network. These damage the image of the brand and creates the impression that the price at which the goods are sold are not the right one. However, the worst affected parties from grey market activity are the retailers whose substantial investments are undermined.

The phenomenal rise of online sales affects consumers because grey market products are being sold next to counterfeit goods at similar prices which creates confusion for clients. When this occurs with luxury food and drink products or beauty and fragrance products, there is a substantial health and safety risk.

With regard to active sales, suppliers can currently prevent existing authorised resellers from selling to unauthorised parties. That must be retained but could we would invite the CMA to consider allowing restricting sales from outside the territory or restraining sales inside the territory to unauthorised distributors? That is already available for selective distribution systems but could be extended to other distribution systems. If that is a step too far then potentially a solution could be for the law to restrain unauthorised distributors from soliciting or even acquiring products that they should not have.

We would also welcome guidance which stated it was acceptable for a brand owner to require information from re-sellers about the identity of customers and transactional volumes with a view to identifying the source of grey market sales or that it may restrain further sales to resellers whom they reasonably consider to be failing to prevent grey market sales.

It should also be noted in a grey market context that Post Brexit, the Intellectual Property (Exhaustion of Rights) (EU Exit) Regulations 2019 provides that from 1 January 2021, intellectual property rights in goods put on the market in the EEA will be exhausted in the UK but there is no such reciprocity for goods put on the market in the UK (i.e. putting the goods on the market in the UK will not exhaust the IP rights in the EEA). This means that whilst owners of UK intellectual property rights cannot prevent parallel imports from the EEA, as the UK is no longer a Member State, owners of IP rights in the EEA are able to prevent parallel imports from the UK. This poses an acute threat to the owners of brands and the value of their related marks, particularly if they cannot restrain grey market sales.

In relation to passive sales, there is a current presumption all internet sales are passive. The internet has moved on since then and a possibility to target groups of companies, especially when sales techniques using social media are studied. We would, as pointed out elsewhere in these responses, invite the CMA to reconsider the presumption set out at para 52 of the VGL that all sales are passive and instead use a case by case analysis to determine whether a sale is active or passive using territory specific criteria.

Specifically within the context of the UK, we would invite the CMA to consider allowing a restraint of sales outside the territory where this is necessary to ensure goods are sold in compliance with applicable local rules. For example, with regard to the considerations linked to the Northern Ireland Protocol, we urge the CMA to set out in guidance that it is permitted for suppliers to impose territorial bans where this is intended to ensure that goods are sold in compliance with local marketing regulations. Northern Ireland for many purposes remains part of the EU's single market and may be subject to diverging trading regulations. It would be legitimate for a brand owner to take steps to ensure that its goods are not sold in any way which would contravene local trading rules as that would reflect prejudicially on the brand and the manufacturer itself.

With regard to added flexibility in distribution systems, it would be useful for the CMA to include some commentary in relation to multi-tiered distribution systems involving a master distributor. For example, the retained VBER/VGL are unclear on the possibility of appointing a wholesale "master distributor" on an exclusive basis within a member state and task that master distributor with finding and managing selective distributors to sell goods at a retail level in the territory.

We also consider that the guidance could confirm the ability of a manufacturer to require resellers to stock the full range of its goods rather than focus on a limited number of best-sellers where it considers this appropriate.

**Question 22: Do you have any examples of circumstances where territorial and customer restrictions might lead to operational efficiencies? Please include examples of locations within the UK and, where possible, quantitative and/or qualitative evidence in your answer.**

The best example of how this is selective distribution systems. By their nature, they restrain the flow of goods outside the authorised distribution network. However, they create operational efficiencies by ensuring that goods are sold appropriately, thereby enhancing the value of goods and strengthening interbrand competition. Operational efficiencies are achieved for the manufacturer by limiting the different points of sale to a smaller number of appropriately equipped and qualified resellers.

We believe it is also well documented that the allocation of exclusive territories to distributors may incentivise them to make brand specific investments such as advertising in order to promote the goods which they are tasked to resell. The rules on active and passive sales as set out in the retained VBER strike a balance which protects exclusivity appropriately. This principle has been recognised throughout several iterations of previous vertical block exemptions and in decisions of the EU Commission. We have set out elsewhere that there is a case for restraining active and passive sales in cases where there may as a result be sales of goods which are not in accordance with the applicable local selling rules.

**Question 23: How helpful is the exemption for restrictions of active sales in the UK to your business or those you represent? Please explain your answer.**

- a) Very helpful**
- b) Somewhat helpful**
- c) Irrelevant**
- d) Unhelpful**
- e) Very unhelpful**

The ban on active sales is extremely helpful in assisting businesses to structure distribution systems which are effective. From a manufacturer's perspective, there may be operational efficiencies involved in dealing with an exclusive distributor or a network of selective distributors as a single point of sale where the distributor has the necessary competence and skill to sell the goods appropriately. The balance struck is the right one insofar as it allows the restraint of active sales where the brand owner has a legitimate interest to preserve such a restraint (i.e. where they have either reserved the territory for themselves or have allocated a territory or customer group to a distributor on an exclusive basis) while also preserving consumer choice.

We feel it would be useful to provide further guidance on the following points:

- What it means for a brand owner / manufacturer to "reserve a territory" to itself (i.e. what level of evidence is needed to show it has been so reserved?)
- The meaning of "customer group" and the characteristics or criteria that can be applied in order to identify a customer group. For example, a manufacturer may define a customer group by reference to "customers shopping online" and allocate that group to itself or another exclusive distributor which may curtail the ability of other resellers to sell online if they had not been allocated that particular notional customer group.

### **Policy questions**

**Question 24: What are your views on the CMA's proposed recommendation on dual pricing and on the equivalence principle?**

We are in agreement with the CMA's recommendations in both areas for the reasons set out below.

#### Dual Pricing

We consider dual pricing to be a useful tool to allow manufacturers to seek to level the playing field between online retailers and bricks and mortar resellers. We are aware of instances where retailers' willingness to make brand specific investments has been chilled by the presence of lower cost resellers who are able to undercut them. Retailers who concentrate on internet based sales will almost universally enjoy a lighter cost base which will put them at a competitive advantage relative to traditional resellers.

#### Equivalence (selective distribution)

Regarding the requirement of "equivalence", when the rules on selective distribution were devised, the internet was in its infancy. E-commerce needed protection. These days, bricks and mortar channels are more in need of protection than online outlets.

Our members consider that it is critical for brand owners to ensure consistency in standards between the way in which goods are sold in stores and how they are sold online. Ultimately, the question of what is consistent should be a matter for brand owners. It must be remembered that they will only benefit from the safe harbour to the extent their market share (and that of the reseller) falls below the 30% threshold.

Requiring absolute equivalence is unhelpful. It should be for the brand owner to decide what is necessary in order to protect the brand and preserve the aura. As mentioned above, they will wish to ensure consistency in standards as a matter of protecting the goodwill in their brand. It is not helpful that their judgment could be subject to legal review on the vexed question of whether there is an equivalency between the standards imposed for offline and online sales.

We consider that requiring absolute equivalence may also get in the way of the creation of innovative omnichannel consumer experiences. One of our members described how they are using a cutting edge omnichannel experience which relies on augmented reality to create a more exciting and enjoyable customer experience in-store. This illustrated how the online experience is not seeking to replicate the offline sales experience but to complement it. The overall result, however, is an enhanced consumer experience. Mandating absolute equivalence may thwart the ability to design a distribution system in which online and offline channels play distinct but integrated roles.

Given the strong consumer demand for online sales, it can be expected that brand owners cannot afford to impose conditions on internet sales which would significantly preclude this type of sales channel.

It should also be possible for brand owners to require similar investments by internet sellers as those made by brick and mortar resellers. It is important to maintain the principles of the **Coty** judgment in English Law.

**Question 25: Do you agree that additional guidance on this issue would be helpful? If so, please provide your views on what that guidance should say.**

With regard to dual pricing, it would be helpful for the CMA to set out in guidance that it is permitted for parties to charge higher prices for internet sales in order to protect offline sales. We would urge the CMA to allow manufacturers a margin of discretion to decide for themselves how to evaluate the cost base and redress the inherent advantages of selling online rather than to seek to prescribe in detail how they should make those assessments or quantify costs.

### **Impact questions**

**Question 26: What are your views on the current regime, which treats certain online sales as a form of passive sales? What are some examples of the benefits or costs for your business operations, or the operations of those you represent? Please include examples and where possible, quantitative and/or qualitative evidence in your answer.**

We consider that this classification is outdated and largely fails to reflect the commercial reality. The original categorisation was made at a time when using the internet selling was novel. That is no longer the case and furthermore internet selling techniques have become more sophisticated.

It is generally unhelpful to brand owners to have this classification as it makes it more risky to regulate internet sales by distributors. Abolishing the “equivalency” requirement, as we have proposed elsewhere, would go some way to addressing the issue.

## Coty judgment

As we have stated previously, Walpole members are particularly keen to ensure coherence of their brand image and customer experience. frequently impossible for owners of luxury brands to maintain the aura of luxury surrounding their goods if these are resold on certain platforms that do not offer the qualitative environment necessary for maintaining the luxury aura of such goods and which, in addition, free-ride of the qualitative investments made by the brands and their authorised retailers. Sales on such platforms frequently juxtapose luxury goods next to lower quality items, which has a highly counterproductive effect in terms of allowing the supplier of luxury goods to create the right image for its brand. Platforms, in our members' experience, are frequently the venue for the sale of counterfeit goods and fail to meet the qualitative criteria observed by other authorised resellers. Moreover, because the brands have no direct contractual relationship with the platforms, it is impossible for the brands to ensure the platforms respect those criteria.

The CJEU, in Case C-230/16 **Coty Germany GmbH v Parfümerie Akzente GmbH** rendered a long-awaited final judgment confirming the permissibility of platform bans on re-sellers in the context of selective distribution systems and ruled without ambiguity that, within the specific context of luxury goods, a marketplace ban imposed by a supplier in a selective distribution agreement falls outside the scope of Article 101(1) TFEU if it is necessary to preserve the quality and proper use of the products in question.

The CJEU also recognised in this judgment that the prohibition on sales via third party online marketplaces would afford the supplier to ensure goods are only associated with its authorised retailers and thus that those goods are sold in an environment which meets the appropriate qualitative conditions and standards. It also confirmed that these rights are essential for suppliers as they otherwise have no contractual relationship with the third party platform which would allow them to control the way in which goods were sold on the platform. The CJEU concluded that the aura of luxury is one of the expectations consumers have with regard to luxury goods and that this expectation would clearly be tarnished by unregulated sales on third party platforms.

The consensus amongst those Walpole members whom we have consulted is that the principles of the *Coty* judgment must be upheld in English law and incorporated into the new VGL which will accompany the UK VBEO. We consider it important to ensure that brands can protect their image by restraining platform sales where necessary. That is an important element in order to attract inward investment from overseas brands and protect the investments of those authorised re-sellers who invest sufficiently in offline sales to ensure experimental, luxury environments which create the aura of luxury which must accompany the goods and allow consumers to have a physical experience of the products, accompanied by adequate advice which they can reasonably expect with regard to such products. It also does not restrict the choices of consumers as the same resellers are authorised to sell the goods concerned online, offering consumers a qualitative environment in which they can be confident that they are receiving authentic, traceable and up-to-date products, accompanied by relevant high-quality services, on- and offline.

**Question 27: Does the treatment of online sales bans as a hardcore restriction have an overall positive or negative impact on your business? Where possible, please provide examples of the impact on online channels and offline channels in your answer. Please include qualitative and/or quantitative evidence where possible.**

- a) Significant positive impact
- b) Moderate positive impact
- c) Negligible impact
- d) Moderate negative impact
- e) Significant negative impact

It is generally in the interests of consumers to allow brand owners to devise sales channels which are adapted to their needs. Whilst we would not advocate allowing brand owners to impose outright sales bans, they may occasionally be justified. We consider that it would be useful for the CMA to give expanded guidance on when outright sales bans may be permissible. We think the CMA can take considerable comfort from the huge customer demand for the ability to access goods and services online insofar as it would be suicidal for many brand owners or manufacturers to entirely prohibit their re-sellers from selling online. The likely result would be a loss of market share for the brand and reduced revenues.

This question is distinct from the question of banning sales on online platforms, which we have addressed elsewhere. For our members, it is important to preserve the ability to restrain the sale of goods on online platforms where the conditions of the *Coty* judgment are met.

**Question 28: Do you consider that the CMA's proposed recommendation (to remove dual pricing and the requirement for overall equivalence in selective distribution from the list of hardcore restrictions) will benefit offline channels? If yes, please provide examples where possible**

We are strongly of the view that such a move would strongly benefit offline sales channels. This would enhance the ability of the brand owner to protect offline sales channels from free riding by predominantly online sellers and redress the inherent cost structure advantage enjoyed by online sellers. Dual pricing will be a helpful tool to assist in the preservation of bricks and mortar stores and the vibrancy of the UK High Street. We also consider that this will assist in protecting high quality jobs in physical stores which could otherwise be lost.

#### **Policy question**

**Question 38: The CMA invites views on the above proposed recommendation in respect of agency issues and stakeholders to make any submissions they consider would help the CMA to develop useful guidance on this topic**

We agree with the representations made to the CMA that the guidelines on agency (as set out in the current VGL) could be clearer in relation to online relationships. Much of the guideline content had been written in the pre-internet era and would benefit from updating.

The definition of genuine agency relies on whether or not the bulk of the risk of customer transactions is borne with the principal or agent. We recognise that defining genuine agency is an immensely complex task. Clarity could be added by the CMA providing a more specific explanation of risk allocation in the context of online transactions (e.g. where a customer's credit card fails to yield payment, should the risk be borne by the principal in a genuine agency relationship?)

In terms of the specific guidance for online sales, it would be helpful for the CMA to review the different elements of an internet sales transaction and try to contextualise its guidance with reference to as many of those elements as possible. For example, the question of whether or not the agent bears the risk of a non-payment following a credit card failure in the context of an online sale may be relevant to the definition. The VGL has a tendency at times to draw on one or two disparate examples to illustrate a wider legal principle. It would be helpful if the CMA could adopt a more comprehensive approach, looking at each of the most common hallmarks of an internet based sale.

## Sustainability

### Policy question

**Question 39: The CMA invites views on the above proposed recommendation in respect of environmental sustainability and stakeholders to make any submissions they consider would help the CMA to develop useful guidance on this topic.**

We agree with the proposals of the CMA in relation to sustainability. Sustainability criteria are an important part of the current business environment. For many luxury brands, it is important that they not only adopt high ESG related standards themselves, but also ensure that those standards are adopted by their trading partners. This is demonstrated by the Walpole Sustainability Manifesto (available here: [WALPOLE LAUNCHES BRITISH LUXURY SUSTAINABILITY MANIFESTO | \(thewalpole.co.uk\)](https://thewalpole.co.uk)) which has been wholeheartedly endorsed by our members.

With regard to selective distribution systems, brand owners may only impose standards to the extent that these are proportionate. That may invite arguments that ESG standards, which some may view as extraneous to the quality of the goods all the environment in which they are sold, go beyond what is necessary for a supplier to require. We think that it would be helpful therefore for the CMA to set out explicitly in its guidance that it is legitimate for brand owners to require distributors to meet ESG related criteria as a condition of admission into a selective distribution system.

We would urge the CMA to look more broadly at the concept of sustainability. There is evidence that both consumers and investors include **human rights** and **ethical production of products**. A survey carried out by Deloitte (available here: [Sustainable Consumer | Deloitte UK](#)) indicated that two thirds of customers pay attention to ethical working practices and human rights issues when they shop for clothes and footwear.

That consumers are concerned to avoid products or services tainted with **modern slavery or human trafficking** is reflected in the passage of the Modern Slavery Act 2015. Section 54 of that Act requires corporate entities above a certain size to disclose annually the steps they are taking to ensure there is no modern slavery within their organisation or supply chain. With this in mind, we would propose that the new VGL could make clear that suppliers can impose requirements on distributors to require them to take steps to ensure they are not implicated directly or indirectly in forced labour or human trafficking.

Further research by McKinsey (available here: [Survey: Consumer sentiment on sustainability in fashion | McKinsey](#)) on attitudes towards consumers of fashion items reached similar findings to the Deloitte study. That study illustrated that:

- nearly 90% of consumers believe that more attention needs to be paid to reducing pollution,
- around two thirds of consumers, see it as more important to limit the climate impacts in the wake of Covid 19;

- 63% of consumers consider a brands action on sustainability as an important purchasing factor;
- 79% of global consumers say they include sustainable packaging in their purchasing decisions;
- 65% of consumers reporting intentions to buy more high quality, durable products.

## Impact questions

**Question 40: What are your views, if any, on whether the retained VABER and EU Vertical Guidelines, contain or frustrate initiatives which might support the UK’s Net Zero and environmental sustainability goals. Please include examples to support your views where possible.**

As indicated above, we feel that the VGL could be clearer as to the legitimacy of the use of sustainability related criteria in relation to the admission of resellers into a selective distribution system. Criteria applied must be “proportionate” which could lead to arguments about whether ESG related criteria are sufficiently linked to the subject matter of the selective distribution system.

In the context of public procurement, similar issues were raised in the case of *Case C-513/99, Concordia Bus Finland Oy Ab, formerly Stagecoach Finland Oy Ab v Helsingin kaupunki and HKL-Bussiliikenne* where the claimant questioned whether the application of certain environmental criteria was relevant or legitimate in the selection of a contracting partner for the supply of bus services. The European Court of Justice has said that this would only be justified where there was a clear linkage between the environmental criteria used and the subject matter of the contract. The use of guidance will help head off similar arguments arising in the context of competition law. Such arguments may well be made where, for example, a distributor is terminated on environmental grounds.

Incidentally, we also note that HM Government has proposed to reform UK Public Procurement Law, inter alia, to make it easier for public bodies to include environmental considerations within award criteria for contracts. The changes proposed by the CMA in the context of competition law are in step with that legislative direction.

**Question 41: Relative to the current regime, would any amendments relating to environmental sustainability (either in the UK VABEO or any CMA VABEO Guidance) have a positive impact on your business’s operations, or the operations of those you represent? Please provide examples and evidence where possible about how any such amendments would have a positive impact.**

We reference our answer to Question 40. The proposals by the CMA would bring welcome legal certainty and avoid potentially contentious issues between suppliers and distributors.

**Question 42: Relative to the current position, would any amendments relating to environmental sustainability (either in the UK VABEO or any CMA VABEO Guidance) have a negative impact on your business’s operations, or the operations of those you represent? Please provide examples and evidence where possible about how any such amendments would have a negative impact**

As with the issue of equivalency, we consider that it would be appropriate for the brand owner to have discretion to set environmental criteria as they see fit, which may in some cases become a matter of negotiation with resellers. We would not think it appropriate for the CMA to dictate in its guidance what specific criteria would be appropriate (e.g. carbon emissions targets). It may be appropriate for manufacturers to reference industry schemes related to ESG criteria in their own criteria. However, they should be able to refer to other criteria as well if they considered that to be appropriate.



**Follow-up**

We trust this input will assist the CMA in its continued consideration in relation to the UK VBEO and the accompanying guidelines which will follow. Walpole looks forward to inputting into the CMA's continued work in this area and remains at the disposal of the CMA should you have any follow-up questions on any of the points we have raised.