Annexes to the CMA's recommendation

Annex A: Legal framework

Chapter I prohibition

1. The Chapter I prohibition (section 2 of the Act) prohibits agreements between undertakings, decisions by associations of undertakings or concerted practices which have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom and may affect trade within the United Kingdom, unless they meet the conditions for exemption contained in section 9(1) of the Act.

Exemption regime

2. Section 9(1) of the Act specifies that an agreement is exempt from the Chapter I prohibition if it:

   (a) contributes to

   - (i) improving production or distribution, or

   - (ii) promoting technical or economic progress,

   (b) while allowing consumers a fair share of the resulting benefit; and

   (c) does not

   - (i) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; or

   - (ii) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

3. Under section 6(1) of the Act if agreements which fall under a particular category of agreements are, in the opinion of the CMA, likely to be exempt agreements, the CMA may recommend that the Secretary of State make an order specifying that category for the purposes of this section.

4. Under section 8(1) of the Act, before making a recommendation under section 6(1), the CMA must:

   (a) publish details of its proposed recommendation in such a way as it thinks most suitable for bringing it to the attention of those likely to be affected; and

   (b) consider any representations about it which are made to it.

Retained VABER[1]

5. The retained VABER relates to agreements between two or more undertakings that, for the purpose of the agreement, operate at different levels of the distribution or production chain and relate to the conditions under which the parties may purchase, sell or resell certain goods or services (vertical agreements).[2] Such vertical agreements are indispensable to many sectors of the economy.

6. The retained VABER exempts from the Chapter I prohibition categories of vertical agreements and concerted practices which are assumed to confer sufficient benefits to outweigh any potentially anti-competitive effects.[3] By virtue of satisfying the conditions of the retained VABER, such vertical agreements are automatically exempt from the Chapter I prohibition.

7. The retained VABER is one of the 'retained exemptions' created by a combination of the operation of the European Union (Withdrawal) Act 2018 and the Competition (Amendment etc.) (EU Exit) Regulations 2019.[4] Since the end of the Transition Period (1 January 2021) the retained VABER has provided certain agreements with an exemption from the Chapter I prohibition, meaning that:

   (a) agreements benefiting from the EU VBER before 1 January 2021 continue to be exempt from the Chapter I prohibition under the retained VABER, provided they continue to meet the criteria of the retained VABER; and

   (b) agreements entered into from 1 January 2021 are exempt from the Chapter I prohibition under the retained VABER, provided they meet the criteria of the retained VABER.[5]

Application of the retained VABER

8. **Exemption**. Article 2 of the retained VABER exempts vertical agreements, subject to the following provisions contained in the retained VABER.

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[1] Available at https://www.legislation.gov.uk/eur/2010/330/contents
Please note the outstanding changes introduced by the Competition (Amendment etc.) (EU Exit) Regulations 2019 not yet incorporated into this published version of the retained VABER.
[2] Article 1(1)(a) of the retained VABER.
[3] See EU Vertical Guidelines, paragraph 108.
[4] As amended by the Competition (Amendment etc.) (EU Exit) Regulations 2020.
[5] See paragraph 4.31 of the Brexit guidance.

9. **Market share threshold**. The parties to the vertical agreement under consideration must have market shares of 30% or less on the relevant market (Article 3). Parties can refer to Article 7 for guidance on applying the market share threshold.

10. **Hardcore restrictions**. The vertical agreement must not contain any hardcore restrictions (Article 4). If a vertical agreement contains a hardcore restriction, the entire agreement falls outside of the retained VABER and must be assessed under the Chapter I prohibition. Given the seriousness of hardcore restrictions, there is a presumption that they fall within the Chapter I prohibition and are unlikely to satisfy the conditions for individual exemption in section 9 of the Act. Parties are, however, entitled to submit efficiency claims to demonstrate pro-competitive efficiencies that outweigh the likely harm.

11. **Excluded restrictions**. The vertical agreement must not contain any excluded restrictions (Article 5). If excluded restrictions can be severed, the remaining vertical agreement may still benefit from the retained VABER.

> By way of example, Company A is a manufacturer of blodgets with a 28% share of sales across the blodget market. Company B is a retailer of blodgets and has a 15% share of all blodget purchases made. The two companies enter into an agreement for the supply of blodgets by Company A to Company B. The vertical agreement requires Company B to purchase all of its blodget requirements from Company A for the duration of the vertical agreement, which lasts for 10 years. The vertical agreement also requires Company B to sell blodgets for no less than £5. Company A does not operate a selective or exclusive distribution system.
>
> a) Company A and Company B satisfy the market share thresholds contained in Article 3. Therefore, their vertical agreement satisfies Article 2 subject to Articles 4 and 5 of the retained VABER.
>
> b) The requirement for Company B to purchase all blodget requirements from Company A is a non-compete obligation, because Company B cannot purchase blodgets from any of Company A's competing suppliers. This is an excluded restriction under Article 5 because the vertical agreement lasts for 10 years. The vertical agreement can still benefit from the retained VABER (subject to any hardcore restrictions – discussed below) if the provision is removed from the agreement or the duration of the agreement is reduced to 5 years.

c) The requirement for Company B to price blodgets at £5 or more amounts to RPM because it stipulates a minimum sale price. This is a hardcore restriction under Article 4(a). The entire agreement cannot benefit from the retained VABER unless this provision is removed. As a result, the agreement would be individually assessed under the Chapter I prohibition.

Withdrawal of the retained VABER

12. The CMA is entitled to withdraw the benefit of the retained VABER in respect of individual agreements under section 10(5)(d) of the Act.[6]

13. The Secretary of State is entitled to vary or revoke the retained VABER pursuant to section 10A of the Act. This includes revoking the retained VABER in relation to parallel networks of similar vertical agreements covering more than 50% of a given market.[7]

[6] See also The Competition Act 1998 (Competition and Markets Authority's Rules) Order 2014, Rule 15.
[7] This power was maintained post-Transition Period by the Competition (Amendment etc.) (EU Exit) Regulations 2019 (as amended), Schedule 3, Part 2, paragraph 10.

Annex B: Alternative policy options

1. The CMA does not recommend that the Secretary of State either:

   (a) allows the retained VABER to lapse on its expiry on 31 May 2022; or

   (b) renews without varying the retained VABER for any period.

Lapse

2. Vertical agreements are recognised as having many positive benefits, such as optimising supply chains and promoting improved quality of services.[8] Without the retained VABER or any UK ORDER, parties would have to individually self-assess every vertical agreement for compliance with Chapter I of the Act. A UK ORDER would instead exempt certain categories of vertical agreements, such that an individual self-assessment is not required.

3. Individual self-assessments can place a considerable burden on both the CMA, national courts, and parties to vertical agreements.

4. Parties can rely on the enforcement practice of the CMA and the European Commission as well as the existing case law of the UK and European courts.[9] However, such decisions and judgments are case-specific and cannot always be directly applied, which limits the degree of legal certainty they provide.

5. The CMA focuses its efforts on deterring and influencing behaviour that poses the greatest threat to consumer welfare, weighing up the merits of each investigation according to its impact on consumer welfare and wider economy, strategic significance, risks and resources required.[10] The occupation of the resources of the CMA to assess individually a wide-range of vertical agreements would undermine the CMA's ability to pursue this strategically targeted enforcement approach as well as adequately resource its other functions. The objectives of a block exemption for vertical agreements are:

   (a) facilitating self-assessment of vertical agreements by providing greater legal certainty as to which agreements can be considered compliant with

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[8] EU Vertical Guidelines, paragraph 33.

[9] The CMA and UK courts will continue to have regard to European Commission decisions made prior to EU exit (section 60A(3) of the Act). Subject to exceptions contained in section 60A(4) to (7) of the Act, the CMA and UK courts will ensure no inconsistency between UK decisions following EU exit and any EU court decisions prior to EU exit (section 60A(1) to (2) of the Act).

[10] See the CMA's Prioritisation Principles (CMA16), available on Prioritisation principles for the CMA (publishing.service.gov.uk)

Chapter I of the Act and which agreements require an individual assessment; and

(b) avoiding the risk of false positives or false negatives by ensuring that only those agreements which it can be assumed with sufficient certainty fulfil the conditions of section 9(1) of the Act are exempted.

6. If the retained VABER is allowed to lapse on expiry, parties to vertical agreements previously exempted under the retained VABER would need to assess the compliance of all vertical agreements with Chapter I of the Act under section 9(1) of the Act.

7. Such individual assessment would bring some benefits:

(a) Parties would enjoy increased flexibility with the ability to design their distribution systems in view of their own assessment of the risks of an infringement of the Chapter I prohibition.

(b) The CMA would be able to individually assess any vertical restraints, which may be helpful in capturing agreements which would have fallen within the retained VABER or a UK ORDER but nonetheless have a detrimental impact on competition. This may be particularly valuable for any new types of vertical restraints arising as the UK market continues to evolve.

8. Allowing the retained VABER to lapse could also result in the following disadvantages:

(a) A reduction in legal certainty for parties to vertical agreements and a corresponding increase in compliance costs.

(b) An increase in the resources that the CMA and the courts would need to devote to assess a wider range of vertical agreements, undermining its ability to focus on those vertical agreements with a greater likelihood of competitive harm.

(c) The lack of a 'safe harbour' for categories of vertical agreements that are considered likely to satisfy the requirements for exemption under section 9 of the Act[11] could have a chilling effect on businesses' incentives to enter into vertical agreements that are likely to generate consumer

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[11] See **Annex A: Legal framework** for these requirements.

benefits, for example through promoting efficiencies, non-price competition, investment and innovation.

9. The CMA considers that the disadvantages of allowing the retained VABER to lapse (paragraph 8) outweigh the benefits of such policy option (paragraph 7). Overall, the evidence gathered in the context of the CMA roundtables, the EU Evaluation and the responses to the CMA's consultation shows that a vertical agreements block exemption is a relevant and useful tool for businesses, providing legal certainty for common types of commercial agreements that pose no significant harm to competition. The vast majority of respondents to the CMA's consultation, from across different industries and sectors, agreed that that the CMA should recommend to the Secretary of State that he should make a Block Exemption Order to replace the retained VABER, rather than letting it lapse without replacement or renewing without varying it.[12]

10. The CMA therefore considers that letting the retained VABER expire without providing for a replacement is not currently appropriate in the UK. Indeed, it is beneficial to have a 'safe harbour' for categories of vertical agreements that are considered likely to satisfy the requirements for exemption under section 9 of the Act[13] because such agreements are likely to generate consumer benefits, for example through promoting efficiencies, non-price competition, and investment and innovation.[14]

Renew without varying

11. Since the European Commission's adoption of the EU VBER on 1 June 2010, there have been various changes in the UK market, primarily linked to the increasing digitalisation of the UK economy, which have been mirrored by developments in applicable case law, as well as the CMA's and European Commission's decisional practice. These changes have affected the distribution and pricing strategies of both suppliers and distributors.

12. Market changes that have been observed include the exponential growth of online sales, increased price transparency and monitoring, access to a wider customer base, increased direct-to-customer sales, and a rise in the use of

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[12] L'Oréal, British Glass, Richemont, Walpole, Anonymous 1, SMMT, Addleshaw Goddard, Eversheds Sutherland, VBB, K&L Gates, ECCIA, Freshfields Bruckhaus Deringer, Brands for Europe, Travelport, Amazon, EU Travel Tech, ABI, ABA Antitrust Law and International Law Sections, Which?, BBC, City of London Law Society Competition Law Committee, In-house Competition Lawyer's Association, British Brands Group, NFDA, Joint Working Party of the Bars and Law Societies of the United Kingdom (JWP) and Gowling.

[13] See **Annex A: Legal framework** for these requirements.

[14] Notably, before the UK and EU systems of competition were aligned on 1 May 2004, the vast majority of vertical agreements were excluded from the application of competition law in the UK under the UK Exclusion Order, made under section 50 of the Act. The UK Exclusion Order had only one 'hardcore' restriction, which related to price-fixing.

selective distribution systems. There has also been a rise in the number of online platforms acting as intermediaries and/or making direct sales.

13. As a result of changes in the market, it is likely to be helpful to businesses for the current regime under the retained VABER to be brought up to date in a UK ORDER for the purposes of legal certainty.[15]

14. The CMA has concluded that the current regime for the vertical agreements block exemption should be revised in certain respects, and that it would not be appropriate simply to renew the existing retained VABER in its current form. In particular, respondents to the CMA's consultation have underlined several areas where the retained VABER could be brought up-to-date to reflect market conditions better.[16] Such views were also expressed by stakeholders in the EU Evaluation, which identified several issues with regard to the functioning of the current rules.[17]

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[15] As mentioned above, the vast majority of respondents to the CMA's consultation, from across different industries and sectors, agreed that that the CMA should recommend to the Secretary of State that he should make a Block Exemption Order to replace the retained VABER, rather than letting it lapse without replacement or renewing without varying it.

[16] In Sections 4 to 9 of the CMA's recommendation, the CMA sets out detailed analysis of its proposed changes to the current regime, as well as its views on areas in respect of which it is not proposing changes.

[17] Evaluation SWD, pp75, 106 and 114.

Annex C: Evidence gathering

The EU Evaluation

1. The European Commission launched an evaluation on 3 October 2018 with the aim of gathering evidence on the functioning of the EU VBER and the EU Vertical Guidelines. The scope of the European Commission's evaluation comprised all member states of the EU (which at the time included the UK). Its evaluation included the decisional practice of member states' national competition authorities ('**NCAs**') (including the CMA) and the European Commission as well as the relevant jurisprudence of national (including UK) and European courts.

2. The European Commission used the following sources: a public consultation; a targeted NCA consultation; a stakeholder workshop; an evaluation support study; spontaneous stakeholder submissions; and evidence gathered through other initiatives.[18] The limitations of the analysis included difficulties in gathering evidence on EU VBER related costs and benefits, a certain lack of representativeness of stakeholder feedback, and a lack of information about consumer views.[19]

Evidence gathered by the CMA

3. The CMA gathered evidence by inviting interested parties to share their views, in particular on any UK-specific issues relating to the retained VABER and the EU Vertical Guidelines. The CMA invited views from:

   (a) businesses with operations in the UK that rely on the retained VABER (for example, suppliers of goods and services, distributors/retailers of goods and services, and platforms/intermediaries active in e-commerce);

   (b) professional advisers (law firms and economists) who advise businesses on the application of competition law to vertical agreements in the UK;

   (c) industry associations; and

   (d) consumer organisations with an interest in the UK market.

4. The CMA has hosted five roundtables and four bilateral meetings with interested parties between 29 March 2021 and 11 June 2021. The CMA has also received a number of written submissions from interested parties. These

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[18] Evaluation SWD, section 4.1 on pp 22-25.
[19] Evaluation SWD, section 4.3 on pp 27-29.

have been used by the CMA when considering its recommendation to the Secretary of the State. The views expressed are summarised below.[20]

Dual distribution

Retention of the dual distribution exception

5. A common theme emerging from the CMA roundtables was support for retaining the exception from the general rule in Article 2(4) of the retained VABER for dual distribution in any UK vertical agreement block exemption. Participants said that several market changes (including the trend of online customers that has been accelerated by the Coronavirus (COVID-19) pandemic) have made manufacturers consider increasing their involvement in distribution. Some participants queried how dual distribution should apply to online platforms.

6. Several participants were of the opinion that removal of the exception would be detrimental. They suggested that, given the prevalence of dual distribution, there would be a high cost for suppliers changing their existing arrangements if they were to choose between vertical integration and independent sellers. Hence, they reasoned that there would be a huge practical impact on businesses if the exception were removed, as contract agreements would need largescale review adding complexity with little benefit to the consumer.

7. It was also suggested that the removal of the exception would fundamentally disrupt the distribution setup of the UK. It was noted that it is beneficial for retailers and direct sellers to both have access to the market as they can attract different consumers and increase market penetration.

8. However, some participants, particularly representatives from the automotive sector, were generally more critical of the retained VABER, with one participant suggesting that dual distribution should not be covered by the block exemption and should instead be fully addressed under the horizontal framework.

Role of information flows in dual distribution

9. Another common theme from the CMA roundtables was that further guidance relating to ‘information exchange’ issues is needed. In particular, it was

[20] The present Annex does not purport to be an exhaustive record or compilation of all the views expressed by participants. Instead it attempts to summarise the key, high-level points made by participants. This summary does not constitute a reflection of the CMA’s position in respect of the issues which were discussed. The CMA’s representatives chaired and attended the various roundtables to listen to the views of participants.

suggested that guidance on the specific circumstances in which the provision of information in a dual distribution scenario would be capable of giving rise to competition concerns from the CMA's perspective would be helpful. There was also discussion on whether these information flows should be considered ancillary to a dual distribution relationship or should be a separate horizontal consideration.

10. Participants noted that there were ways to address the issues surrounding the flow of information within a company (such as through staff compartmentalisation or use of information barriers) but others noted that these could be impractical or impossible for smaller businesses.

11. Other participants noted that data could be legitimately shared between manufacturers and distributors to gain greater knowledge of a supply chain, improve products, and ensure better responses to customer demand. Some participants also questioned the theory of harm relating to this issue. It was suggested that information exchanges in a ‘dual distribution’ scenario, generally form part of the vertical relationship between the supplier and its distributor. It was also noted that the provision of historical information used to understand market dynamics is acceptable.

12. However, other participants recognised that the provision of information had the potential to be problematic and smaller firms may suffer if there is not sufficient clarity regarding the provision of information. It was noted that it is sometimes difficult to distinguish between a pro-competitive vertical exchange of information and an anti-competitive horizontal exchange.

13. Some participants, particularly representatives from the automotive sector, raised concerns over manufacturers’ ability to gain unfair access to information from retailers (such as detailed information on their sales and margins) which could grant the manufacturer a competitive advantage if they chose to enter the market as a retailer.

Addition of a lower market share threshold

14. Participants were generally not in favour of introducing market share thresholds as they considered that this would add complexity for businesses. In particular, it was noted that a need to ascertain a company’s market share would be possible for larger businesses but not smaller firms.

Extension of the dual distribution exception to other types of firms

15. Some participants noted that the extension of the exception for dual distribution to wholesalers, importers and distributors is needed as there is currently a situation where, if such firms decide to sell directly, then their agreements with resellers potentially fall outside the scope of the block exemption.

Retail Price Maintenance

16. Participants noted that there are circumstances in which RPM may be problematic, for example:

    (a) where there are networks of agreements such that RPM is prevalent across a particular market; or

    (b) where RPM is agreed between parties with market power, as this has greater potential to affect inter-brand competition, including, for example, where downstream retailers with joint market power use RPM to preserve the status quo and prevent the emergence of new business models.

17. Other participants noted that the theories of harm for RPM were relatively specific, and that RPM should only be considered problematic when it affects inter-brand competition.

18. Participants (both at the CMA roundtables and in bilateral meetings) provided the following examples of when efficiencies may arise from RPM:

    (a) for new product launches, although there were differing views regarding the permissible duration of RPM;

    (b) for seasonal or high-end products;

    (c) to prevent free-riding, for example, where bricks-and-mortar outlets invest heavily in quality or service;

    (d) for common promotions in franchising models;

    (e) to prevent products being used as ‘loss leaders’ or ’traffic generators’;

    (f) to maintain brand value during the lifecycle of a product; and

    (g) to test the positioning of a product in a market.

19. Some participants (particularly economists) said that RPM should not be categorised as a hardcore restriction and instead an ‘economic effects’

approach would be more appropriate. Some participants pointed to the more effects-based treatment of RPM in certain other jurisdictions.

20. Other participants said that the current regime should not be revised. Several participants (both at the CMA roundtables and in written submissions) suggested that further worked examples of the circumstances in which RPM may be justified would be useful. Participants also suggested that guidance in the context of franchising arrangements would be helpful.

21. Some participants observed that under the current regime businesses may be unwilling to engage in RPM because of the risks involved even in circumstances where they consider it overall pro-competitive. Other participants said that it is important to consider the way in which efficiency arguments are assessed in any particular case, alongside the appropriate categorisation of RPM under any block exemption. Participants suggested that a possible option may be to encourage firms to seek short-form opinions from the CMA on specific cases or the provision of clear guidance and worked examples.

22. Finally, participants (both at the CMA roundtables and in written submissions) said that further guidance on a number of other issues would be useful:

- determining the permissibility of recommended resale prices (particularly in the context of parties with higher market shares);
- the assessment of fulfilment contracts (or 'flash title transfer'), including in the context of logistics or sales facilitation services; and
- the assessment of the collection by suppliers of retail pricing data from their retail distributors.

Territorial and customer restrictions

Exclusivity

23. A few participants suggested that businesses should have the ability to restrict active sales and allocate different territories to different distributors. One participant noted that, in some sectors, absolute territorial protection may be justified by network complexities and the need for local economies of scale.

24. It was noted, however, that allowing absolute territorial and customer restrictions could have unintended consequences such as certain consumers in the UK being unable to use a shop or service in a part of the UK where they do not live.

Combining distribution models

25. There was general agreement that the current rules were somewhat inflexible and forced businesses to be cautious by either entering into a fully selective or fully exclusive distribution model in order to benefit from the block exemption. This prevents businesses from adopting alternative pro-competitive arrangements that do not fall squarely into the 'exclusive' or 'selective' distribution categories.

26. Participants said that territorial sales restrictions were less viable outside of exclusive distribution networks. They were in favour of more flexibility for businesses to choose their own route to market as it was difficult for businesses to reconcile the current rules with what they wanted to do in terms of distribution.

27. Many participants were in favour of a more permissive system that allowed businesses to combine different models at different levels of the supply chain. A suggestion was made to allow the combination of exclusivity at the wholesale level with selective distribution at the retail level. It was noted that such a change would provide flexibility and greater legal certainty for businesses wishing to adopt such distribution models.

Shared exclusivity

28. Another common theme which emerged from the CMA roundtables was businesses' aspiration to have the ability to appoint more than one distributor per exclusive territory whilst still benefitting from the block exemption. According to some participants, allowing 'shared exclusivity' would lead to significant efficiencies by spreading risk across more than one distributor, ensuring wider distribution and bolstering intra-brand competition. They noted that shared exclusivity was currently avoided due to the inability to prevent active sales into territories where there is more than one distributor.

Extraterritorial restrictions and Northern Ireland

29. Participants called for more clarity as to whether businesses could impose territorial restrictions between the UK and the EU, especially considering the possible implications of the Northern Ireland Protocol.

30. Participants explained that there were legitimate reasons to prevent the re-import of goods due, for example, to the different standards between states as regards, for example, labelling and language requirements. Participants also noted possible issues around intellectual property, trademark exhaustion and differing trading standards. It was noted that the current approach to export

bans was brought about to protect the EU singe market and some participants did not understand the theory of harm outside of this particular context.

31. When considering the possible implications of the Northern Ireland Protocol, participants noted that businesses were unfamiliar with the possible consideration of different parts of the UK as different markets and that this approach could lead to burdensome management arrangements for businesses.

32. Participants were of the view that it would be helpful to have more clarity around the possible scenarios where a supplier operating a selective distribution model across Europe may lawfully restrict sales from outside the territory to unauthorised distributors within the UK.

Online sales bans

33. Participants were sceptical that any firm would have an incentive to fully restrict online sales given the importance of this distribution channel as a route to market. According to those participants, rather than restricting online sales, brand owners might want to have the ability to incentivise the sale of goods from physical stores.

34. It was suggested by some participants that some online restrictions were artefacts of an earlier age and that flexibility regarding efficiencies is needed if online sales bans were to remain hardcore restrictions.

35. Other participants suggested that if non-dominant businesses wanted to attempt to restrict online sales this would be a self-inflicted risk due to the importance of the online sales channel. It was also mentioned that those businesses should be entitled to ignore or control online sales as they see fit. However, it was noted that, if online sales were subject to increased restrictions, certain geographic areas within the UK without access to brick-and-mortar stores could experience exacerbated geographic market issues.

The distinction between active and passive sales

36. Participants questioned the conceptual distinction between active and passive sales. They queried whether the perceived strict approach to online sales was still justified given that online sales no longer needed the same protection due to the growth in online sales in recent years and the increased capability to target specific groups of online consumers.

37. It was suggested that the distinction was no longer relevant outside of the context of the EU single market imperative. It was also noted that there is only a competition concern where the parties to the vertical agreement have

market power and, when this is the case, the distinction between active and passive sales becomes irrelevant.

38. On the other hand, it was noted in a written submission that the distinction between active and passive sales is well understood and provides a workable differentiator between lawful and unlawful restrictions in individual cases. It was recognised that, despite the challenges in the distinction between active and passive selling, it remained useful.

39. It was also suggested that any CMA guidance on this issue should reflect recent case law and decisional practice, including the European Court of Justice judgment in *Coty*[21] and the European Commission decision in *Guess.*[22] This would improve legal certainty and prevent inconsistency of approach across relevant authorities.

Other issues

40. Participants, especially those representing luxury brands, expressed the view that the integrity of selective distribution should not be compromised by any future changes to the rules. It was noted that quality-based selective distribution systems were permitted in the European Court of Justice judgment in *Coty* and participants wanted to see this, and other recent case law, incorporated into any CMA guidance.

41. Some participants suggested that suppliers should have the ability to require distributors to provide information about their customers where they were caught reselling. Those participants were in favour of introducing restrictions on active and passive sales to those customers facilitating 'grey market' sales.

Indirect measures restricting online sales

The exponential growth of online sales

42. Participants agreed that online channels had grown significantly over the last decade and no longer required the level of protection afforded to them under the current regime. It was noted that the current guidelines were introduced when internet sales were still taking shape but in the current climate, if anything, brick-and-mortar stores were the distribution channel in need of protection.

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[21] *Coty Germany GmbH v Parfümerie Akzente GmbH* (Case C-230/16) EU:C:2017:941.
[22] See Commission press release of 24 July 2018, IP 18/4601, available here. A non-confidential version of the prohibition decisions is available on DG Competition's website.

43. Participants recognised that brick-and-mortar retailers were facing increasing challenges when competing against online channels, a situation which was further exacerbated by the restrictions placed on retail premises as a result of the Coronavirus (COVID-19) pandemic.

Brick-and-mortar distribution channels

44. There was broad agreement that there should be scope to be more permissive in relation to what brand owners can do to encourage investments made by bricks-and-mortar retailers without necessarily disrupting online retailers.

45. Participants were of the view that businesses desired more flexibility to reward investments made by brick-and-mortar retailers or otherwise incentivise the sale of goods from physical stores. Recognising that physical retail stores incur much higher costs than pure online distributors, participants stated that brands wanted to support brick-and-mortar stores but there was a perception that it was difficult to fully compensate or reward investments in those stores under the current VBER rules.

46. Participants acknowledged that the EU Vertical Guidelines did allow for some incentives to be given in order to reward investments in brick-and-mortar distribution. However, it was suggested that these mechanisms were not particularly utilised because they did not reflect the complexity of many commercial arrangements, or implied the need to monitor the costs of authorised dealers; something which was regarded by participants as impractical.

47. Participants agreed that significant investment was required for brick-and-mortar stores and that brands should be able to provide additional rebates, discounts and support, or, at least, more than a mere lump sum payment to fully reward investments in physical stores, marketing or broader efforts for the brand.

Omni-channel distribution

48. Many participants stated that both online and brick-and-mortar channels were important for the businesses they represent. Consumers utilised both channels in both directions (offline to online, as well as online to offline) in their decision-making processes. These businesses were therefore committed to an omni-channel distribution and would not have any incentives to restrict online sales, even if they were allowed to do so.

Equivalence principle

49. Participants suggested that offline and online channels served different purposes and had different methods of securing consumer purchases. It was also noted that not all services offered in store could be offered online. In this regard, brands had practical difficulties in developing equivalent criteria for two very different sales environments.

50. Taking into account that these channels serve completely different purposes, there was wide agreement amongst participants that full equivalence was not possible in every single case and that the equivalence principle was somehow out of tune with current market conditions. Some participants stated that, if the equivalence principle were to be relaxed (ie removed as hardcore restriction of competition), this would enable greater optimisation of performance within these differing channels. The CMA has received a written submission in which the opposite view was held. In this submission it was noted that despite the challenges presented by the equivalence principle, it still remained a useful and coherent guide for self-assessment.

51. Some participants stated that, in their industries, the protection of luxury brand 'aura' was of critical importance and therefore it was crucial for their businesses to maintain control over what was shown to customers online.

52. The importance of the requirement for proportionality (as per the *Metro* criteria[23]) in any assessment of the equivalence criteria between brick-and-mortar and online distribution was mentioned, and it was suggested that it would be helpful to have more guidance on these criteria.

Dual Pricing

53. Many participants agreed that the relaxation of the rules on dual pricing would help businesses encourage investments in bricks-and-mortar channels. It was therefore suggested that the any CMA guidance on the issue should not treat dual pricing as a hardcore restriction and set out examples of when dual pricing would cease to benefit from exemption. In a written submission it was mentioned that it would be beneficial to allow variable promotional support in some circumstances.

[23] Case 26/76 *Metro v Commission* (No 1) [1977] ECR 1875, EU:C:1977:167.

Parity obligations

54. There were a range of views amongst participants regarding direct and indirect sales channel parity obligations but there was a consensus that more clarity on the treatment of these clauses was needed.

55. The discussion was largely dominated by indirect sales channel parity obligations (also referred to as 'wide most favoured nation' clauses) and participants generally agreed that these typically give rise to more competition concerns than direct sales channel parity obligations (also referred to as 'narrow most favoured nation' clauses).

Theories of harm: indirect sales channel parity obligations

56. Many participants agreed that indirect sales parity obligations were particularly problematic when in widespread use and/or employed by businesses with significant market power.

57. It was noted that the extent of harm from a particular type of sales channel parity obligation depends on the importance of the parameter of competition that the parity obligation relates to.

58. Participants made the following points regarding the possible theories of harm on the use of indirect sales channel parity obligations:

- finding the same price across all platforms due to parity clauses leads to the avoidance of price competition;
- platforms were able to charge high fees and there was little evidence of fee cutting, which indicated that sales channel parity clauses were dampening the incentives for platforms to compete;
- if allowed, sales channel parity clauses for online platforms would create a similar competitive landscape as RPM did for retail, which is currently prevented and viewed as harmful regardless of any market share thresholds; and
- indirect sales channel parity clauses could prevent entry of new platforms and businesses from creating new offerings.

Efficiencies: indirect sales channel parity obligations

59. Participants recognised possible efficiency justifications for indirect sales channel parity obligations. There was a general consensus among

participants that the avoidance of free-riding was the main justification used for online platforms (eg consumers may gather all the information needed to make their choice on a comprehensive online platform and then go to another platform to book at a cheaper rate).

60. It was also mentioned that indirect sales channel parity obligations could lead to the following efficiencies:

- reduced consumer search costs if prices are the same across channels;
- increased consumer trust in online platforms if consumers are not able to find a better price on other channels;
- reduced negotiation costs between suppliers and platforms;
- facilitation of new entry; and
- avoidance of free riding by alternative channels.

61. Regarding the avoidance of free riding, other participants were sceptical about the relevance of this factor and suggested that:

- any free-riding issues were likely to be minimal because the amount of investment required for platforms paled in comparison to investments made by the businesses who provided the actual goods and services; and
- any free-riding issues may be mitigated as a result of other competitive factors such as revenue generated by platforms obtaining and utilising data from customers.

Inclusion in the UK ORDER and/or the CMA Verticals Guidance

62. Some participants suggested that they would like to see sales parity obligations codified within the block exemption regulation itself while others saw merit in addressing them within the any future guidelines.

63. Participants called for more legal certainty through an update to the guidelines to reflect recent case law.

64. In relation to the future treatment of sales parity obligations there were mixed views. A few participants expressed scepticism that parity obligations merited much attention at all with regards to the retained VABER, as the circumstances in which they are problematic were narrow and becoming clearer with current case law. They were comfortable with the provision of a safe harbour for sales parity clauses employed by businesses with a market

share below 30%. Another participant stated that at least indirect sales channel parity obligations should not benefit from safe harbour at all.

65. It was also suggested by some participants that parity clauses should be subject to an effects-based analysis and a ‘by object’ type of categorisation should be avoided.

66. In general, participants were more comfortable with the idea of creating a safe harbour for direct sales channel parity obligations than for indirect sales channel parity obligations. Participants generally agreed that whichever direction the CMA takes, clear guidance with examples was crucial. Some participants called on the CMA to not only focus on market shares but also to provide additional guidance on market definition which was perceived to be a complex exercise in some cases.

67. Some participants noted that any hard stance taken by the CMA would be rendered pointless if online platforms were to remain able to replicate the effect of parity clauses by means other than parity clauses, for example by penalising non-compliant suppliers through ranking changes.

Wholesale parity obligations

68. Participants who opined on wholesale parity obligations generally agreed that they were less problematic in the absence of market power and that additional guidance would be helpful.

69. A further participant noted that they tended to be problematic in a very limited set of circumstances and clarified that the problematic ones could be dealt with outside of the retained VABER context because either (i) the parties exceeded the market share cap or (ii) the parity obligations could be categorised as contractual provisions in horizontal rather than vertical agreements.

Other issues

70. It was noted that businesses were increasingly raising concerns around non-price parity provisions and that therefore the CMA should provide guidance on how these can be assessed. It was suggested that a non-price term could be assessed by looking at whether it was a competitive factor in the given marketplace.

Non-compete obligations

Duration of non-compete obligations

71. One of the issues that the CMA roundtables focused on was the most suitable length of non-compete obligations, both generally and within specific sectors. Some participants suggested that the five-year limit generally worked well as it provided certainty and gave businesses the chance to re-evaluate their market position. One participant suggested that businesses would generally opt for the exempted length provided in any UK vertical block exemption.

72. Other participants suggested that the ideal length of a non-compete obligation varied by sector. For example, it was suggested that bancassurance was a sector where five years was too short a length of time to be efficient, while five years was probably too long for agreements in the technology sector. One participant suggested that high initial set-up costs incurred by a distributor or franchisee could justify a non-compete obligation of up to ten years.

73. It was also noted that issues with the five-year timeframe were irrelevant in the context of franchising. Another participant added that non-compete obligations that did not cover 100% of a given buyer's purchases should be allowed to extend beyond five years. One participant raised that, while the five-year requirement was not ideal, a divergence between the EU and UK on the legal basis for non-compete obligations was undesirable.

74. In contrast, one participant questioned whether non-compete obligations should even be covered by the 'safe harbour', as there could be concerns with these obligations even under five years. One participant representing the automotive sector argued against a more permissive approach to non-competes, supporting that manufacturers already exerted undue influence over dealers and had restricted dealers operating multi-brand showrooms.[24] This participant suggested dealers were subject to strong manufacturer influence towards the end of a five-year agreement.

75. Finally, a common theme emerging from a number of the CMA roundtables was that market shares and market power were more important factors than duration in analysing the impact of a non-compete obligation, and that an agreement where firms had under a 30% market share would have limited effects, even over five years. Other participants suggested that the retained

[24] Article 3 of the Commission Regulation (EU) No 461/2010 (the Motor Vehicle Block Exemption Regulation)read in conjunction with Article 5(1)(a) of the EU VBER permits suppliers and distributors with a share of the relevant market not above 30% to agree on a single-branding obligation (see supplementary guidelines on vertical restraints in agreements for the sale and repair of motor vehicles and for the distribution of spare parts for motor vehicles , paragraph 26).

VABER, with its reliance on the 30% market share threshold, does not always accurately reflect or capture the balance of power in non-compete relationships.

Tacit renewal of non-compete obligations

76. Several participants suggested that a requirement to renegotiate any non-compete obligation every five years felt mechanistic, artificial, arbitrary, or did not reflect commercial reality. It was suggested that tacitly renewable non-compete obligations exceeding five years should not be an excluded restriction, and that these could also be efficiency-enhancing. Some participants also requested a more flexible approach, suggesting that an ability for either party to terminate the (tacitly renewable) obligation at any point would be sufficient, absent significant market shares.

Post-term non-compete obligations

77. Two participants suggested that additional clarity and guidance regarding ongoing investments related to know-how (such as in training or intellectual property) was needed. It was also argued that, as the conditions regulating post-term non-compete obligations relate only to premises rather than exclusive or non-exclusive territory, they were ill-suited to the UK market, where services-based franchises and distribution arrangements were more predominant than in EU markets.

Other Issues

78. It was noted that the block exemption does not currently apply to any direct or indirect obligation causing the members of a selective distribution system not to sell the brands of particular competing suppliers. One participant suggested that this requirement felt artificial in practice and should be removed from any future version of the retained VABER. It was also suggested that further CMA guidance is needed on clauses that are treated as, or act as, non-compete obligations in practice such as ‘English clauses’, minimum purchase requirements and exclusive purchase obligations.

Agency

General

79. Some participants considered that the guidance on the definition and assessment of agency in the EU Vertical Guidelines is useful,[25] whilst others considered that clarifications were needed. In particular, participants considered that any guidance accompanying the UK ORDER should be updated to reflect current commercial realities.

80. Participants (both at the CMA roundtables and in written submissions) suggested the following general revisions to the current regime:

    (a) Further guidance on any grey areas where it is currently unclear if an agency relationship exists (eg where a retailer with strong bargaining power requires a supplier with limited market power to guarantee its margins).

    (b) Further guidance regarding the assessment of relationship-specific risks and sunk investments specific to a brand.

    (c) Additional guidance in the form of worked examples of how agency agreements are to be assessed, including in relation to the assessment of the magnitude of the risk borne by an agent.

    (d) Additional guidance on agency issues in the context of franchise relationships.

    (e) Additional guidance on the assessment of agency arrangements in the context of modern platforms and distribution models. It was noted by some participants that as business models become more innovative, a broader definition of agency allowing for greater flexibility would be welcome. Several participants suggested that there should be a move away from the current focus on the allocation of risk, whilst others considered that risk allocation remains an important determinant.

81. Some participants noted that there are differing perspectives on the definition of agency arrangements between lawyers and economists (based on differing

[25] Participants of the Automotive sector roundtable thought that the EU Vertical Guidelines are generally helpful, especially in carefully considering the concept of risk and the definition of genuine agents. It is also straightforward to differentiate between agency for competition law purposes as compared to the commercial definition of agency.

perspectives on risk allocation in the context of an undertaking), which should be borne in mind.

82. Finally, one participant noted that agency agreements provide businesses with flexibility and that there is a risk that distorting the definition of such arrangements to cover too much would ultimately lead to the benefits being lost. One participant said that it may not be appropriate to codify case law in any guidance as it could quickly become outdated given the fast-changing nature of commercial models. Another participant noted that although more flexibility would be useful, it was more important that any guidance increases legal certainty in relation to the definition and assessment of agency agreements.

Online platforms

83. Participants considered that clarifications to the current regime were required to address their application to agreements with online platforms, particularly given the rise of the internet as a channel for selling goods. In particular, some participants considered that platforms should be categorised neither as agents nor retailers, but instead as a third category of undertaking. Other participants suggested that some specific examples relevant to online sales would be helpful, particularly on how risk is allocated across the elements of online transactions.

84. Participants explained that it can be difficult to apply the traditional definitions of agency to online platforms. Participants noted the following points:

- platforms generally impose terms on suppliers, which is the opposite of what is traditionally the case in agency relationships; and
- parity clauses (which may arise in agreements with online platforms) generally benefit the platform and not the supplier and can diminish competition between platforms with a profound effect on suppliers.

Fulfilment contracts

85. Participants considered that clarifications to the current regime were required to address the application of agency to fulfilment contracts, where a party takes title of the goods when providing a service for the supplier (eg logistics or operating the supplier’s website). Participants generally considered that this model is currently caught by the Chapter I prohibition even though any negotiation regarding price takes place between the supplier and end-customer (ie the intermediary sells at the price requested by the supplier according to the contract between the supplier and end-customer).

86. Some participants noted that in some instances, the retailer requires the supplier to use a particular logistics company to deliver the goods, so the intermediary relationship is dictated by the retailer. Participants considered that the rules preventing the supplier from imposing a price on the third-party logistics provider (on the basis that they are not an agent as they have taken full risk over the goods for delivery purposes) do not reflect the commercial reality of the negotiation.

Dual-role agents

87. Participants considered that clarifications to the current regime were required to address the application to so called ‘dual role agents’ (where companies act as independent distributors for certain products and as agents for other products for the same supplier), the use of which is emerging in the automotive, financial services and other sectors.

88. In written submissions some participants suggested that any CMA guidance should confirm that the agency aspects of such arrangements can fall outside of the Chapter I prohibition. However, other participants considered the use of dual role agents to be unfair as manufacturers choose which products to prioritise for the agency route, whilst relying on retailer investment for sales of other products.

89. Participants were also concerned that this practice allowed manufacturers to control retail prices whilst potentially pushing more risk onto agents or former resellers. Participants said that the parameters of intra-brand competition (especially on price) were diminished by pushing more sales through the agency route.

90. Finally, it was suggested that some guidance on cost allocation in the context of dual role agents would be useful (ie how to accurately allocate costs to a partner in their capacity as independent distributor versus as an agent).

Environmental sustainability

91. The general observation made at the CMA roundtables was that environmental sustainability is a theme that is mostly discussed in the context of horizontal agreements. It was also noted that there was no consensus on what fell under the term ‘sustainability’ as it could include social impacts (eg fair wages and working conditions).

92. Participants noted however that environmental sustainability is of strategic importance for businesses and consumers, and that manufacturers/brands

have shown interest in becoming 'greener', for example by wanting their retail networks and distribution systems to accept packaging returns.

Use of sustainability commitments and obligations as selection criteria in a selective distribution system and for assessment under section 9 of the Act

93. Participants noted that any CMA guidance could usefully set out how sustainability commitments and obligations could be used as selection criteria in a selective distribution system and how this would be assessed under Section 9 of the Act.

94. Participants asked specifically for more guidance on how environmental criteria could be imposed in selective distribution where such criteria may not be necessary for the provision of the goods or services in question. This point was further developed in the context of purely qualitative selective distribution system, in a written submission.

Out-of-market efficiencies

95. Participants raised out-of-market efficiencies as a special case of efficiencies and suggested that competition policy could be a good tool in this area. It was noted that most of these efficiencies might be rooted in the negative externalities of these agreements, which may make them difficult to assess (eg to quantify the benefits).

96. The general consensus was that out-of-market efficiencies should be considered by competition authorities when reviewing agreements under Chapter I of the Act. In particular, one participant noted that most of the benefits of sustainability enhancing agreements were to society as a whole and thus out-of-market.

97. One participant suggested there may be a connection between out-of-market efficiencies and non-price parity clauses, which could be a way to address the potential market failure in which consumers could not credibly interrogate the sustainability of a supply chain.

98. One participant noted that in a vertical relationship, the seller could simply impose minimum quality standards downstream which are unlikely to cause competition concerns.