

## RETAINED VERTICAL AGREEMENTS BLOCK EXEMPTION REGULATION

### CONSULTATION ON THE PROPOSED RECOMMENDATION TO THE SECRETARY OF STATE

#### RESPONSE BY GOWLING WLG (UK) LLP

We welcome the opportunity to respond to the consultation on the proposed recommendation by the CMA that the Secretary of State replaces the retained Vertical Agreements Block Exemption Regulation (the "**retained VABER**")<sup>1</sup> with a UK Vertical Agreements Block Exemption Order (the "**UK VABEO**").

#### Policy and impact

**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?**

1 Yes.

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

2 In our experience, businesses place a clear value upon the availability of defined "safe harbours" from the general prohibition of section 2 of the Competition Act 1998 (the "**Chapter I Prohibition**"). The existence of such safe harbours, including under the retained VABER, provides businesses with the choice either to:

- (a) cast their arrangements to fall within the scope of those safe harbours, with a significant number of commercial arrangements structured to benefit from the certainty of an available safe harbour; or
- (b) operate outside of these safe harbours, having self-assessed the compatibility of the relevant arrangements with the Chapter I Prohibition.

3 We anticipate that the UK VABEO, together with accompanying guidance (the "**CMA VABEO Guidance**"), will provide greater clarity and certainty for businesses, in relation to both the availability of the safe harbour across a range of different distribution models, as well as with regard to the principles for self-assessment outside of the scope of the safe harbour.

4 We believe that this greater clarity and certainty will encourage investment, and stimulate innovation and competition within the UK, with businesses utilising combinations of sales channels to maximise their reach, increasing the profile of their brands and products, and customers and consumers benefitting from greater choice and access to products.

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<sup>1</sup> Whereby, pursuant to Regulation 3(9) of The Competition (Amendment etc.) (EU Exit) Regulations 2019, at the end of the Brexit Transition Period, Commission Regulation No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices was retained in an amended form (i.e. the retained VABER), together with the accompanying guidance relevant to the interpretation of the VABER, the Commission Notice – Guidelines on Vertical Restraints (the "**Vertical Guidelines**").

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

5 Significant positive impact.

**Dual distribution**

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

6 We welcome the CMA's proposed recommendation that the UK VABEO includes an exception for dual distribution, and that this is extended to apply to wholesalers and importers.

7 We do not consider that a horizontal market share threshold is required in this context, given that this would introduce unnecessary complexity and uncertainty to an issue that businesses are already addressing, and are well able to continue to address.

**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.**

8 As noted above, businesses are already addressing this issue, and will continue to be able to self-assess potential concerns. However, in order to further assist businesses, we consider that the CMA VABEO Guidance should:

(a) confirm that information exchanges in dual distribution scenarios are generally capable of benefitting from the UK VABEO; and

(b) define any specific circumstances when such information exchanges could give rise to concerns from the CMA's perspective, and confirm the types of safeguards that the CMA would expect businesses to consider putting in place to address these concerns.<sup>2</sup>

**Resale price maintenance**

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

9 We note the CMA's proposal in relation to RPM remaining a "hardcore" restriction of competition under the UK VABEO.

10 However, we believe that the CMA VABEO Guidance should provide examples of circumstances in which RPM could be compatible with the Chapter I Prohibition.<sup>3</sup>

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<sup>2</sup> See, by analogy, "Interim measures in merger investigations, 28 June 2019, CMA108", paragraphs 3.15 – 3.18.

<sup>3</sup> We note that the current proposal is for the CMA VABEO Guidance to clarify that the CMA "*remains open to carefully and objectively considering any efficiency arguments made in the course of any investigations*" (see, paragraph 4.11 of the Consultation document).

**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.**

- 11 As noted above, we believe that the CMA VABEO Guidance should provide examples of circumstances in which RPM could be compatible with the Chapter I Prohibition (e.g. in the context of certain short-term promotional activities across distribution networks).
- 12 We also believe that the CMA VABEO Guidance should confirm that, in the context of fulfilment contracts, an agreement between a supplier and a third party, pursuant to which the third party will purchase and resell products to enable the fulfilment of the supplier's commercial agreement with its customer (i.e. where the resale price has already been agreed between the supplier and its customer) would not constitute RPM (see, response to Question 38 below).

**Territorial and customer restrictions**

**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.**
- 13 We welcome the CMA's proposed recommendation in relation to territorial and customer restrictions, particularly with regard to the following aspects being permitted under the UK VABEO:

- (a) combining exclusive and selective distribution at different levels of the supply chain in the same or different territories;
- (b) sharing "exclusivity" in a territory, or for a customer group, by allowing the allocation of a territory or customer group to more than one "exclusive" distributor; and
- (c) providing greater protection for members of selective distribution systems against sales being made into the relevant territory by unauthorised resellers from outside the territory (together, "**Permitted Restrictions**").

14 We also welcome the proposed inclusion within the UK VABEO of definitions of "active sales" and "passive sales".

**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.**

15 We agree that additional guidance would be helpful, particularly in relation to:

- (a) confirming the CMA's approach to the interpretation of "active sales", and "passive sales", including in the context of online sales, and online sales strategies;
- (b) confirming the availability of the UK VABEO with regard to each of the Permitted Restrictions;
- (c) if any of the Permitted Restrictions was to fall outside of the safe harbour of the UK VABEO, confirming the circumstances in which each of the Permitted Restrictions:
  - (i) would generally be compatible with the Chapter I Prohibition; and
  - (ii) could give rise to concerns from the CMA's perspective; and
- (d) more generally, confirming the ability of a supplier to limit a reseller's physical place of establishment (e.g. an outlet and/or a warehouse) to a specific address approved by the supplier, irrespective of the distribution model(s) utilised by the supplier.

#### **Indirect measures restricting online sales**

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

16 We agree with the CMA's proposed recommendation that the following should cease to be treated as "hardcore" restrictions of competition under the UK VABEO:

- (a) charging resellers higher prices for products to be resold online, as compared to when the same products are to be resold offline ("**dual pricing**"); and

- (b) imposing criteria for online sales which are not equivalent overall to the criteria imposed in brick-and-mortar stores in the context of selective distribution ("**non-equivalent sales criteria**").

17 We consider that this proposal acknowledges the significance of e-commerce as a sales channel, and the need to provide businesses with the flexibility to adapt their strategies to utilise online and offline sales channels as efficiently as possible.

**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.**

18 We agree that additional guidance would be helpful, including in relation to:

- (a) confirming the availability of the UK VABEO with regard to the use of dual pricing, and/or non-equivalent sales criteria; and
- (b) if the use of dual pricing and/or non-equivalent sales criteria was to fall outside of the safe harbour of the UK VABEO, confirming the circumstances in which each aspect:
  - (i) would generally be compatible with the Chapter I Prohibition; and
  - (ii) could give rise to concerns from the CMA's perspective.

#### **Non-compete obligations**

**Question 34: The CMA invites views on the above proposed recommendation in respect of non-compete obligations. In particular:**

- (a) **Should non-compete obligations that are tacitly renewable remain 'excluded restrictions' under the UK VABEO?**
- (b) **Are there any risks in allowing such obligations to be automatically exempt under the UK VABEO?**
- (c) **Should the current regime in the derogations in Article 5(2) and Article 5(3) of the retained VABER be revised (for example, to reflect market developments such as the increasing trend towards online sales)?**

19 We agree with the CMA's proposed recommendation that non-compete obligations, which are indefinite or exceed five years in duration, should remain excluded restrictions under the UK VABEO.

#### **Agency**

**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.**

- 20 We welcome the CMA's proposed recommendation to provide clarification within the CMA VABEO Guidance in respect of agency agreements, including in the context of "dual role" agency agreements,<sup>4</sup> and fulfilment contracts.
- 21 In our experience, businesses are keen to explore the possibilities of using different distribution models as alternatives to, or in addition to, selective or exclusive distribution models, so as to maximise their reach and increase the profile of their brands and products.
- 22 We therefore believe that the CMA VABEO Guidance should provide accessible, clear guidance (including worked examples) to enable businesses to make informed choices about how they may implement different models in the UK, including:
- (a) confirming how agency agreements are to be assessed for the purposes of the application of the Chapter I Prohibition, particularly in relation to the assessment of the magnitude of the risk borne by an agent;
  - (b) confirming that "dual role" agency agreements can fall outside of the Chapter I Prohibition, and setting out any criteria to be satisfied to achieve this outcome; and
  - (c) confirming how the costs to be paid by the principal (or reimbursed by the principal to the agent) should be calculated and apportioned in the context of an agency agreement, including in circumstances in which:
    - (i) a third party is appointed to act as an agent for the supplier (i.e. with no prior commercial relationship between the third party and the supplier); and
    - (ii) an existing distributor appointed by the supplier (which has made various investments in premises, equipment, and staff training) is then appointed by the supplier to act as its "dual role" agent for a specific range of products (i.e. while continuing to resell the supplier's other products as a distributor); and
  - (d) confirming the circumstances in which an agreement that does not constitute a genuine agency agreement would be compatible with the Chapter I Prohibition, including:
    - (i) where the parties have intended to enter into a genuine agency agreement, but the magnitude of the risk borne by the intended agent is too great; and
    - (ii) in the context of fulfilment contracts, confirming that an agreement between a supplier and a third party, pursuant to which the third party will purchase and resell products to enable the fulfilment of the supplier's commercial agreement with its customer (i.e. where the resale price has already been agreed between the supplier and its customer) would not constitute RPM (see, response to Question 17 above).

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<sup>4</sup> Where companies act as independent distributors for certain products and as agents for other products for the same supplier (see, paragraph 98 of the Consultation document).

### **Environmental sustainability**

**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.**

23 We welcome the CMA's proposed recommendation to provide guidance regarding the circumstances in which environmental sustainability considerations may be used as admission criteria in the context of selective distribution systems.

24 In particular, we consider that the CMA VABEO Guidance should:

- (a) confirm when selection criteria intended to satisfy environmental sustainability commitments and obligations would generally be compatible with the concept of purely qualitative selective distribution; and
- (b) set out any factors that the CMA intends to consider when assessing compatibility in this context.

### **Duration**

**Question 43: The CMA invites views on whether the UK VABEO should have a duration of 6 years.**

25 We agree that a duration of six years would afford the possibility of a timely review of the UK VABEO, ensuring that this remains relevant for UK businesses, customers, and consumers.

### **Other provisions**

**Question 44: The CMA invites views on the above proposed recommendations in respect of the other provisions in the UK VABEO.**

### **Transitional period**

26 We welcome the proposed recommendation to implement a one-year transitional period in relation to the UK VABEO.

### **Subcontracting agreements**

27 Although not addressed within the consultation, we note the reference within the Vertical Guidelines to the Commission notice of 18 December 1978 concerning the assessment of certain subcontracting agreements in relation to Article 85(1) of the EEC Treaty (the "**Subcontracting Notice**").<sup>5</sup>

28 We consider that the Subcontracting Notice provides businesses with a greater degree of certainty as regards the permissibility of certain restrictions when parties are investing in subcontracting relationships.

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<sup>5</sup> See, in particular, Vertical Guidelines, paragraph 22.

- 29 Having regard to the role of the UK VABEO in encouraging investment within the UK, we consider that the CMA VABEO Guidance should also provide certainty in relation to the circumstances in which subcontracting agreements will fall outside of, or be compatible with, the Chapter I Prohibition.

**Gowling WLG (UK) LLP**