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Response to UK Consultation on the retained Vertical Agreements Block Exemption Regulation

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Van Bael & Bellis ("VBB") is an international law firm with offices in Brussels, London and Geneva, having a strong focus on competition law and trade. For more than 30 years, VBB has been advising businesses, organisations and governments on all aspects of EU and UK competition law, and has developed deep expertise in advising clients on all aspects of distribution arrangements and practices.

VBB welcomes the opportunity to be able to contribute to the present Consultation and has found the CMA roundtables over the past few months particularly helpful and productive. VBB looks forward to the next stage of the consultation process and hopes that its views, as expressed below, will be useful to the CMA and other stakeholders.

CMA's proposed recommendation

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

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

In our view, a well-designed, pragmatic, economically sound, and consumer-centred UK block exemption will have a positive impact by significantly increasing legal certainty and reducing compliance costs for all parties involved in the supply chain. This will be even more the case if the accompanying UK VABEO CMA Guidance is also well-drafted and pragmatic.

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

a) Significant positive impact

Associations of undertakings

Policy questions

Question 4: What are your views on the CMA's proposed recommendation for agreements with association of undertakings to continue to benefit from the UK VABEO?

We agree with the CMA's proposed recommendation for such agreements and we believe that they should continue to benefit from the UK VABEO.

Question 5: Do you think that the turnover threshold should be revised for agreements with associations of undertakings to benefit from the UK VABEO (in particular, to reflect market developments, growth, inflation and/or the UK market)? If so, please provide your views on what the new turnover threshold should be.

Although we do not have a strong view on this point, we consider that an appreciable increase of the current threshold is justified in order to cover more businesses and associations. Bearing in mind the size of the UK economy, we would suggest doubling the amount currently covered by the retained VABER as this appears to us to be a step in the right direction.

Impact questions

Question 6: To what extent is the exception for agreements with associations of undertakings, as outlined in the retained VABER, helpful to your business's operations or the operations of those you represent?

b) Somewhat helpful

Question 7: What would be the likely impact on your business's operations or the operations of those you represent if the turnover threshold was increased?

b) Moderate positive impact

Question 8: What would be the likely impact on your business's operations or the operations of those you represent if the turnover threshold was decreased?

d) Moderate negative impact

Dual distribution

Policy questions

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

In general, we agree with the CMA's views and proposed recommendation as dual distribution creates substantial benefits, both for suppliers and for customers.

Dual distribution allows suppliers of branded products to promote their products in an environment that is directly associated with the supplier's brand and reach customers through an additional, complementary sales channel through which suppliers can serve consumers with heterogenous preferences more effectively. Thus, dual distribution can expand consumer choice and more effectively meet consumer expectations. As the CMA has observed, in recent years dual distribution has become very commonplace. In our view, highly competitive retail markets with robust online sales are a very strong indication of the competitive benefits of dual distribution systems. It demonstrates that dual distribution can be an effective way to reach consumer groups with different demands and, therefore, to promote competition and consumer welfare.

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.

Yes, we think that additional guidance in this direction would be helpful, especially if such guidance enhances the ability of suppliers and retailers to collaborate in order to stimulate further (inter-brand) competition and, ultimately, better meet the needs of UK consumers.

It is our experience that information flows - particularly from the retailers to the supplier - continue to raise difficult questions for many market participants, even if purely unilateral. Many stakeholders have pointed out to us the uncertainty and risks which businesses face in this respect. Suppliers commonly seek to address this risk by establishing internal firewalls which prevent sensitive retailer information from reaching those employees who routinely make pricing decisions for the supplier's retail operations. Such information barriers present significant challenges, especially for smaller suppliers, and result in obvious inefficiencies, so should not be viewed as a panacea.

In light of the above, many open questions remain. In particular, there is insufficient guidance on whether, and to what extent, a dual distribution supplier can use potentially sensitive retailer information to inform its overall distribution strategy, and on measures concerning the supplier's internal organisation to prevent unlawful information sharing with those in charge of its retail activities. Such retailers are not competitors to the supplier in the true meaning of the term, but instead they should be viewed as partners of the supplier who are in a position to "compete" against the supplier only because of a non-reciprocal (vertical) distribution agreement. In this regard, we would invite the CMA to clarify the position in its VABEO Guidance on the use of retailer information by a supplier, taking into account the efficiencies that result from the ability of a supplier to have a comprehensive view of consumer demand for its products, including when sold by retailers in the context of a non-reciprocal vertical agreement. A robust case can be made that information necessary for the supplier to co-ordinate the brand propositioning, promotional activities and, more generally, manage a brand's interaction with consumers should be viewed as pro-competitive unless it amounts to resale price maintenance (RPM).

Please also refer to our response to Question 13 below for further arguments supporting our views expressed here.

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

In our view, this exception is vital as it provides more choice to consumers because it addresses different consumer preferences in a constantly evolving omnichannel retail environment. Therefore, we think that the CMA should encourage suppliers to join retailers at their level, and to generally take more control over their market proposition and enhance inter-brand competition which results in offering better prices and quality to consumers. In most (if not all) consumer goods markets in which suppliers generally enjoy no, or at most insignificant, market power, the promotion of inter-brand competition is much more important than intra-brand competition to enhance consumer welfare. Please also refer to our response to Question 13 below for further arguments supporting our views expressed here.

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.

e) Not at all

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.

As noted above, we are certain that dual distribution systems provide significant advantages to suppliers of branded products as well as consumers.

Therefore, removing legal certainty for dual distribution systems by eliminating or limiting the availability of the UK VABEO would not strengthen competition law compliance. To our knowledge, there is no evidence that dual distribution systems result in horizontal competition concerns that would justify any fundamental changes to the current approach. To the extent dual distribution systems could create certain competition law risks (such as collusion at the retail level and unlawful information exchanges that facilitate coordination among the supplier's retail arm and its retail partners), these can already be addressed under the current rules under the Chapter I Prohibition. Changes to the current regime, such as removing the dual distribution exception, would therefore not result in a more effective way to address these concerns.

Moreover, limiting or eliminating the benefits of the UK VABEO for dual distribution would cause enormous uncertainty for many suppliers. The costs of distribution would increase and suppliers may forgo the distribution practices they consider to be most efficient. These effects would be particularly pronounced for selective distribution systems. Today, many suppliers operate selective distribution systems and having to do so without the benefits of the UK VABEO would be extremely challenging.

Despite a supplier's best efforts to self-assess its competition law compliance, any legitimate obligation could be challenged by any retailer who considers the selective distribution system requirements too burdensome. Retailers may become reluctant to join distribution networks or may refuse to share

information. As a result, consumers would suffer. A failure to include the dual distribution exception may even encourage certain suppliers to abandon their dual distribution systems altogether, either by vertically integrating or by abandoning their own retail activities. Either way, there would be less choice for consumers, who would ultimately "pay the price".

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.

We believe that the CMA's proposed recommendation is likely to have a generally positive impact as it will increase legal certainty, especially given that many suppliers not based in the UK would be willing to partner with wholesalers and importers to enhance their presence and offering more generally.

Resale Price Maintenance

Policy questions

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

Credible arguments can be made supporting the view that RPM should be subject to an effects-based analysis and be exempt under the UK VABEO in the absence of a supplier enjoying significant market power, which, in turn, necessitates the countervailing presence of intra-brand competition. However, we understand that it may be difficult for the CMA to fundamentally change the rules in this regard and depart completely from decades of EU and UK jurisprudence.

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.

In our view, RPM efficiencies which could outweigh restrictions of aspects of intra-brand competition are well documented in the economic literature and some US seminal court judgments. Moreover, a subset of such efficiencies was also acknowledged by the European Commission in its Vertical Guidelines and also in the revised draft of the Vertical Guidelines published earlier this month[1]. In our experience, business clients are reluctant to consider, let alone implement, RPM practices, even including the ones identified as acceptable under the EU Vertical Guidelines (e.g. when it comes to the introduction of a new product or service). This is due to the potential risk of bearing high legal and compliance costs, especially costs associated with defending a potential challenge to the otherwise procompetitive RPM practice.

However, when it comes to RPM practices not exhaustively covered by the EU Vertical Guidelines but which can still be procompetitive, business clients have been even more reluctant to implement them given the associated higher legal risk of a challenge by a third-party and the need to defend themselves before a

[1] Please refer to paragraph 182 of the revised draft where it is also acknowledged that RPM may lead to efficiencies in certain cases with concrete examples provided in sub-paragraphs (a)-(c).

competition authority or in court. The other reason is the fact that it is almost impossible to prove that there is no less restrictive practice that is capable of achieving a comparable result under Article 101(3) TFEU (despite that fact that Article 101(3) reverses the burden of proof).

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.

We would absolutely welcome such guidance in light of our response to Question 16 above. In particular, we think it would be extremely helpful if the CMA can expand the guidance on this topic by including examples of RPM practices which can still be procompetitive on balance and thus very unlikely to be susceptible to a successful challenge.

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. In our view, this would lead to the unfettered promotion of beneficial inter-brand competition (when so desired).

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.

Please see our response to Question 17 above. In particular, many businesses are reluctant, if not very reluctant, to consider implementing RPM practices which are on balance procompetitive, due to being very conscious of the associated legal risk, especially the possibility of having to defend a very costly challenge to a practice which, at first glance, may be perceived to be restrictive of competition (and in general perceived as “illegal”), unless the supplier manages to prove otherwise (which, as explained above, has turned out to be very difficult in practice).

<u>Territorial and customer restrictions</u>

Policy questions

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 of the view that an equivalent to the current VABER regime is likely to prove counterproductive within the UK market, and thus businesses should be allowed more flexibility to determine their distribution policies vis-à-vis territorial and customer restrictions. There is no particular reason as to why, in a very well-integrated market, territorial and customer restrictions (in a vertical context), including prohibition of online sales, should be considered hardcore restrictions. Historically, territorial and customer restrictions have been treated with great suspicion in the EEA because of its inherently fragmented market comprised of different nations with different national markets, cultures, languages, etc. It was this particular market structure and the very strong push for the creation of a single market which underpinned the established EU approach. We do not see a reason why UK competition policy should continue to support an approach dictated by the EU Single market imperative.

As a result, we would suggest that territorial restrictions do not necessarily need to be treated as hardcore restrictions and can be well justified in many contexts. For example, if a retailer would like to establish a dealership in a remote UK area, even absolute protection from other dealers may well be justified in order to incentivise the dealer in question to invest in and develop the business successfully.

When it comes to restricting online sales, we are of the view that the supplier should have control over the way products are marketed online. Even if a supplier decides that its distribution should not take place online, contrary to *Pierre Fabre* and *Ping*, we do not see a strong reason why this should not be allowed. Although for almost all of the distribution networks nowadays (and especially following the COVID-19 pandemic), an absolute prohibition on online sales would probably be unpopular, the current approach towards online sales has prevented the emergence of alternative business (and distribution) models. Generally, there may be compelling reasons for the supplier to wish to impose such a ban (e.g., specialised sectors, or high value and/or limited products). If the supplier is prepared to limit the amount of its overall sales by excluding online channels in exchange for other benefits to its business model, it should be allowed the flexibility to do so. Ultimately, and in the absence of significant market power, consumers will decide how and where to buy the product or service in question, which in turn would prove how successful such a strategy would be in practice.

Finally, if the distinction between passive and active sales is to be retained, we believe it is important that all sales strategies which incorporate an "active" element (such as targeted advertising through social media, "AdWords", etc.) should be considered active. On the other hand, passive sales should be the ones which are "100%" passive and it can easily be proven that consumers have actually contacted the retailer in question without any targeted marketing.

Separately, we are of the view that there are other areas where more flexibility can be allowed for under the VABEO as outlined below.

Use of selective and other forms of distribution in the same territory

We are of the view that the current VABER rules are overly restrictive to the extent they limit the circumstances in which a supplier may grant a wholesaler the benefit of full exclusivity (including protection from active sales by other wholesalers) where a selective distribution system is operated at the retail level. Although the VABER does not prevent a supplier from committing to appoint only one wholesaler in a territory and not to sell itself to retailers in a territory (which are partial elements of exclusivity), it does not appear to permit a supplier to restrict active sales to authorised retailers in a wholesaler's territory by other wholesalers located elsewhere.[2]

Currently, such a restriction risks being viewed as a hardcore restriction because it does not appear possible under the VABER to use selective distribution at the retail level and exclusive distribution at another level of trade in the same territory;[3] and, where selective distribution is used at both the wholesale and retail levels, a restriction of active sales by authorised wholesalers to other members of the selective distribution system, including at the retail level, appears to be a hardcore restriction[4].

Therefore, granting a wholesaler full exclusivity where selective distribution is used at the retail level, is normally treated as a serious restriction of competition.

There are often pro-competitive reasons for a supplier to want to grant protection from active sales (and free riding) to wholesalers (appointed to supply authorised retailers) in order to incentivise them to invest and develop the supplier's brand. For example, this may be the case where a wholesaler acts as a national importer for a foreign supplier and coordinates and develops the activities of the brand in a country. What is more, it is generally accepted that any adverse effects which vertical restraints may have on intra-brand competition are likely to be more significant when applied at the retail rather than at the wholesale level. Where there are no territorial restrictions at the retail level, and where, in addition, wholesalers are free (as they must be) to make online and other passive sales in other wholesalers' territories, it is doubtful whether there can be any material risk of undesirable price discrimination. It therefore seems disproportionate to treat such an active sales restriction as a hardcore restriction.

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2 A supplier may only prevent wholesalers located elsewhere from opening a place of establishment in a wholesaler's territory.

3 One reason for this is that a restriction on wholesalers from selling to non-authorised retailers (which would be needed to protect the integrity of the selective distribution system at the retail level) would be a hardcore customer restriction unless the wholesalers would themselves also be members of the selective distribution system (which would enable them to benefit from the limited exception to the treatment of customer restrictions as hardcore restrictions).

4 According to paragraph 58 of the EU VGL, Article 4(d) VBER "*means that an agreement or concerted practice may not have as its direct or indirect object to prevent or restrict the active or passive selling of the contract products between the selected distributors"* and furthermore "[i]*t also means that within a selective distribution network no restrictions can be imposed on appointed wholesalers as regards their sales of the product to appointed retailers.*"

The EU Vertical Guidelines already recognise that active sales restrictions at the wholesale level in a selective distribution system may, in certain circumstances, fulfil the conditions of Article 101(3) TFEU. This may be the case where wholesalers need to carry out promotional activities but where "*it is not practical to specify in a contract the required promotional activities*."[5] We consider this exception to be insufficient: not only is it difficult to assess whether in practice it would be considered to apply (e.g., what exactly would be considered "impractical"), but also, the fact that promotional activities may be specified in wholesaler contracts does not eliminate the risk of free-riding, as those contractually-specified activities may need to be calibrated for different wholesalers. Given the low risk that such restrictions could appreciably restrict competition in the relevant market when agreed by firms with market shares below the modest thresholds of the VABER, and in the absence of judicial rulings suggesting they should be viewed as a restriction by object, there is a strong case to remove them from the list of hardcore restrictions.

Suppliers should have more flexibility to impose active sales restrictions

We believe that the current rules on active sales are too restrictive to achieve the goal of preventing free-riding and that more flexibility is needed. Therefore, suppliers should have more flexibility to impose active sales restrictions.

We would urge the CMA to consider amending the currently very limited circumstances under which an active sales restriction is exempted by the VABER and to allow suppliers more freedom to impose active sales restrictions. The case for such change has now become overwhelming as a result of the exponential growth of online sales – which are treated as passive rather than active sales – that shows no sign of abating. Direct competition from online sales from other distributors means that, in practice, the degree of protection afforded to a distributor by the type of active sales restrictions permitted under the VABER has been substantially diluted over recent years. As a result, there are strong arguments that the restrictive approach of the current rules needs to be relaxed in order for suppliers to be able to incentivise investment (by limiting free riding) even to an extent that was possible under the market conditions that existed when the current rules were adopted. And the competitive pressure now imposed by online (passive) sales means that any such relaxation is highly unlikely to significantly limit even intra-brand competition.

The requirement under the VABER that a distributor may only be restricted from making active sales in territories or to customers that have been either exclusively allocated to another distributor or exclusively reserved to the supplier for direct distribution is already in itself a major limitation. We would urge the CMA to reconsider this approach, which we consider to be excessively strict and which, in our experience, makes it very difficult to ensure that active sales restrictions are in practice exempted by the VABER.

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.

Yes, we would welcome additional guidance in line with our response to Question 20 above.

Impact questions

[5] EU Vertical Guidelines, para. 63.

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.

b) Somewhat helpful

As per one of the examples we have provided in our response to Question 20 above, investment in businesses operating in more remote areas in the UK would likely be incentivised if retailers are allowed to enjoy near-absolute or even absolute protection from other members of the same distribution network.

Indirect measures restricting online sales

Policy questions

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

We generally agree with the CMA's proposed recommendation and we set out below our reasoning in this regard, in more detail. We also provide our views on a number of related points which we hope will be useful to the CMA in the consultation process.

Dual pricing should no longer be treated as a hardcore restriction

In our view, the current prohibition on dual pricing between online and physical retail negatively affects the ability and incentives of retailers to invest in brick-and-mortar (**B&M**) retail and risks contributing to the degradation and disappearance of the added-value services and experiences offered by B&M retail - to the ultimate detriment of consumers.

Under the current framework of the retained VABER, barring dominance, a supplier may unilaterally decide to charge different prices to different wholesale channels or customers. Accordingly, it is open to a non-dominant supplier to charge different prices to pure online and pure B&M retailers, respectively, in order to take account of the higher level of costs borne by B&M retail and thereby provide incentives for pure B&M retailers to invest in their stores and the added-value services and experiences they offer. However, the current treatment of dual pricing as a hardcore restriction leads to a situation where a supplier cannot charge different prices to hybrid retailers (i.e., those with both B&M and online activities) dependent on whether the products are intended for online or B&M resale. This difference in treatment leads to situations where suppliers working with hybrid retailers are unable to effectively take the differing costs of B&M retail compared to online retail into account in their wholesale pricing. This can lead to situations where hybrid retailers focus their attention on online sales and reduce their investments in their B&M activities.

Dual pricing can generate significant consumer benefits

The current EU Vertical Guidelines (para. 52) provide that, while dual pricing will be treated as a hardcore restriction, a supplier may separately support a hybrid retailer's B&M activities through the payment of a fixed fee. While the allowance made for the payment of a fixed fee is useful and allows for the coverage of fixed costs related to B&M activities, it is inflexible, difficult to apply in practice and does not take account

of significant variations in the costs of B&M retail linked to the volume of sales. A fixed fee system is also extraordinarily difficult to implement if a large number of retail outlets carry the supplier's products. By contrast, no longer treating dual pricing as a hardcore restriction would allow the costs of B&M retail to be covered in a more flexible manner that can be implemented more efficiently. This will more effectively preserve the ability and incentives of hybrid retailers to invest in their B&M outlets. In turn, this generates significant consumer benefits through preserving and strengthening the availability of added-value services and experiences through B&M retail.

Of course, consistent with the case law, dual pricing could still be considered a hardcore restriction if it is used by suppliers to prevent hybrid retailers from making online sales. Although we are not persuaded that there is a sound justification for this characterisation, we recognise that the UK VABEO and the CMA VABEO Guidance will have to reflect existing case law. Accordingly, a hardcore restriction may be found where the wholesale price offered to hybrid retailers for products destined for online sale clearly does not allow the hybrid retailer to economically operate online. The CMA should provide further guidance on the interpretation and application of any such safeguards in the VABEO Guidance.

The equivalence principle should no longer apply to criteria applied to online outlets and those applied to B&M outlets

We support removing the "principle of equivalence" from the UK VABEO.

The principle of equivalence is difficult to apply and does not take account of the evolution of retail

While, in principle, such an approach might have been justifiable when the online sales channel was relatively novel and there might have been concerns that not all suppliers would seek to fully utilize the opportunities offered by online sales, in the current retail environment, there is no solid basis for maintaining this approach.

Moreover, in practice, the requirement of equivalence is difficult to apply due to the inherently different character of online selling compared to B&M retail. It is often difficult, if not impossible, for companies and their counsel to reasonably determine whether criteria imposed in relation to online sales are equivalent to those imposed in relation to B&M retail. This results in significant legal uncertainty for companies as to whether their selective distribution systems are compatible with the existing competition rules.

In addition to the inherently different character of online and B&M retail, the growth of "omnichannel" retail strategies (where a brand or supplier's strategy foresees integrated, complementary roles for online and B&M retail) means that brands and suppliers increasingly wish their online and B&M retailers to serve different functions and provide different but complementary services within their distribution systems. As highlighted in the discussion concerning *no longer treating dual pricing as a hardcore restriction*, with safeguards to be defined in line with the case law above, the future of B&M retail appears to be increasingly focused on providing consumers with added-value services and experiences (e.g., high-quality personal pre- and after-sales advice, the possibility to try out and try on products and the ability to interact with brands in a direct experiential way, among many others). These are hands-on services and experiences that online retail is ill-equipped to provide. At the same time, online retail can provide consumers with other, different added-value services and experiences (e.g., in terms of range and choice of products, immersive digital media experiences, social media interaction, etc). Continuing to strictly apply the principle of equivalence

in this context risks stymying the future development of retail formats and preventing brands and retailers taking advantage of the different retail opportunities offered by online and B&M sales, respectively.

The principle of equivalence is no longer necessary to protect online selling

Moreover, as is made clear by the discussion concerning *no longer treating dual pricing as a hardcore restriction*, the principle of equivalence was introduced in the 2010 EU Vertical Guidelines to address concerns that, in the context of selective distribution, brands or suppliers would seek to limit the ability of their retailers to sell online by imposing stricter quality criteria on online sales (compared to B&M sales) at a time when e-commerce was still in the process of establishing itself as a credible and trusted retail channel. The situation today is very different: the internet is a well-established and trusted retail destination and there no longer appears to be any compelling reason to strictly apply the principle of equivalence to protect online selling.

Removing the principle of equivalence can generate consumer benefits

In our view, the UK VABEO should recognise that a brand or supplier can impose different quality requirements on the distribution of their products online and through physical retail, respectively, taking into account the differing yet complementary functions such modes of sale play in an integrated, omnichannel distribution strategy. This could be achieved either through explicitly block-exempting the imposition of different criteria for online and B&M sales in the UK VABEO and/or providing clear guidance on the application of this principle in the VABEO Guidance. While the criteria imposed on online sales should not be such that they effectively prevent such sales, allowing the use of differentiating criteria would protect the legitimate interests of suppliers.

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.

We have set out our views and related suggestions on the issues which should be addressed under the CMA VABEO Guidance in our response to Question 24, above.

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.

Please refer to our response to Question 20 above.

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.

d) Moderate negative impact

Please refer to our response to Question 20 above.

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.

Yes, we do consider that there will be such a benefit – please see our response to Question 24 for more details on this point.

Parity obligations (or 'most favoured nation' clauses)

Policy questions

Question 29: What are your views on the CMA's proposed recommendation on parity (or 'most favoured nation') obligations? As part of this, you might like to consider whether indirect sales channel parity obligations[6] can generate benefits/efficiencies beyond those that may be created by direct sales channel parity obligations[7] – if so, please provide evidence or examples in practice of circumstances where this may be the case.

We agree with some of the CMA's observations and comments on parity obligations, but we disagree on the suggested approach as to the distinction between wide and narrow parity clauses (i.e. indirect vs direct sales channels) and their respective recommended treatment under the UK VABEO. We outline below our reasoning and past experience in this area.

Parity clauses can provide material benefits

Parity obligations are widely used across many sectors of the economy and can offer material benefits to the parties involved. For example, parity obligations can protect retail investments made by a retailer, especially when these investments are dedicated to serving a particular supplier relationship. Parity clauses can also reduce transaction costs as they provide assurance to the buyer that it is obtaining the best possible conditions offered by the supplier on the market without spending additional resources on market intelligence and negotiations. In other cases, parity provisions can protect the interests of a supplier by providing assurance that a powerful retailer will treat the supplier's product no less favourably than those of its rivals, which can facilitate the entry of new market players.

The EC's Final Report on the E-Commerce Sector Inquiry[8] has also recognised that parity clauses can lead to efficiencies similar to some of those described above.[9]

Parity clauses are frequently used other than by digital platforms

Parity clauses are widely used in many industries and generally do not, in our view, distort competition when the relevant agreement otherwise meets the conditions for exemption under the VABER. For example, in our experience parity obligations are often used in the mining industry without generating

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6 As defined in paragraph 4.63 (see document)
7 As defined in paragraph 4.63 (see document)
8 Commission Staff Working Document, COM (2017) 229 final.
9 Ibid. (para. 623).

obvious competition concerns where the VABER applies. It is striking that, with the exception of parity clauses in favour of digital platforms, these clauses have (as far as we aware) been the subject of very few enforcement actions. We are thus not aware of any evidence that parity clauses typically raise competition law concerns.

Furthermore, in almost all cases involving the use of parity clauses by digital platforms, it seems that parity clauses were used in agreements that did not benefit from the VABER because one party's share exceeded 30%.[10] Much of the discussion about the use of parity clauses, and their potential harmful effects on competition, has accordingly focused on the specific environment in which digital platforms operate and the specific effects they may generate in this environment.

In the main cases that have been investigated, the digital platform benefitting from parity clauses typically operated in concentrated markets and arguably had substantial market power. The use of parity clauses in these circumstances may well have created competition concerns, including the risk of upward pressure on prices in the market and the creation of entry barriers.

But these are unique circumstances which, in our view, should not inform possible revisions of the VABER that would apply across all industry sectors. In our view, the evaluation of the current approach to parity clauses under the VABER must not lose sight of the fact that these types of obligations are used in many other contexts where they do not cause concerns and have resulted in very limited enforcement activity.

Therefore, we believe that the exemption under the VABER should continue to cover parity clauses provided that both parties' individual market shares do not exceed 30% and the respective agreement does not contain hardcore restrictions. There is no need to deprive all industry sectors of the benefits and legal certainty offered by the VABER's exemption of parity clauses, especially when used between parties with small or moderate market shares.

Narrow vs wide parity clauses (or direct vs indirect sales channels)

We are also concerned that what may well be the atypical experience provided by the digital platform cases has led the CMA to consider introducing different rules for wide and narrow parity clauses and to apply these rules across all industry sectors.

In previous enforcement cases involving platforms, the majority of NCAs have made a distinction between narrow and wide parity clauses. Some NCAs have concluded that narrow clauses do not restrict competition.[11] By contrast, wide parity clauses (i.e., those that capture all sales channels, including indirect ones) have been consistently considered to raise competition law concerns.[12]

But the context for this distinction has been the digital platform sector, where acute network effects are at play. In our view, it would not be justified to extend the experience from these cases to all other industry

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10 Examples include E-books I (AT.39847), Amazon (E-books II) (AT.40153), Private Motor Insurance (UK CMA, 2015), and the investigation by several NCAs of parity clauses used by Booking.com.

11 See also PMT 13013-16, Booking.com v. Visita, Patent-och marknadsöverdomstolen (Sweden), May 9, 2019. One notable exception to this trend is the Bundeskartellamt, which ruled against narrow price parity clauses in its 2015 infringement decision against Booking.com, currently subject to appeal to the German Federal Court.

12 See, for example, the various decisions by NCAs in Online hotel booking, including in the UK, Germany, France, Italy and Sweden.

sectors. This would merely add further complexity without helping to address generally applicable competition law concerns and would not facilitate or increase competition law compliance.

For these reasons, our view is that the UK VABEO should not make a distinction between narrow and wide parity clauses. We therefore believe the CMA's recommendation to treat wide parity clauses as a hardcore restriction under the UK VABEO, regardless of the industry context and the parties' market shares, to be disproportionate. Instead, we consider it more appropriate for the future VABEO Guidance to provide specific guidance in respect of parity clauses used in agreements where the market share thresholds of the VABER are exceeded, building on the collective experience of the CMA, the European Commission and the NCAs, which have dealt with such cases on previous occasions.

Question 30: Do you agree that additional guidance on this issue would be helpful? If so, please provide your views on what that guidance should say.

We believe that market participants would welcome more clarity on the assessment of parity clauses, especially when used in agreements that do not benefit from the VABER. The CMA VABEO Guidance should therefore, in our view, provide meaningful guidance on the criteria that are relevant to assess the effects of parity clauses in practice.

Impact questions

Question 31: To what extent are indirect sales channel parity obligations relevant for your business's operations, or the operations of those you represent? Please explain your answer.

b) Very much

Question 32: To what extent are direct sales channel parity obligations relevant for your business's operations, or the operations of those you represent? Please explain your answer.

b) Very much

Question 33: Are you aware of any difficulties to your business if indirect sales channel parity obligations are treated as hardcore restrictions for the purposes of the proposed UK VABEO? Please explain your answer.

Yes, we are aware of such difficulties – please refer to our response to Question 29 above.

<u>Non-compete obligations</u>

Policy questions

Question 34: The CMA invites views on the proposed recommendation[13] in respect of non-compete obligations. In particular:

[13] Paragraphs 5.10-5.16.

a) Should non-compete obligations that are tacitly renewable remain 'excluded restrictions' under the UK VABEO?

We are of the view that such non-compete obligations should not continue to be treated as "excluded restrictions", but instead be exempted by the new UK VABEO under the same conditions as any non-hardcore restriction. We do not see any point in preserving the current approach unless the supplier enjoys significant market power. Otherwise, the current approach constitutes an impediment for a supplier with moderate, small or no market presence that desires to invest in a long-term partnership with an established distributor (without having to re-negotiate the clauses for such supplier non-compete provisions at the end of the 5-year period). We have not come across an industry where such non-compete provisions could foreclose suppliers from partnering with distributors and, in any event, if this is indeed the case because of exceptional circumstances or cumulative effects of a network of such non-compete provisions, the benefit of the VABEO can always be removed.

b) Are there any risks in allowing such obligations to be automatically exempt under the UK VABEO?

We do not think there are any such risks in the absence of significant market power, as discussed in the preceding paragraph.

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)?

At this stage, we do not propose any changes to these two provisions.

Impact questions

Question 35: To what extent are non-compete obligations relevant to your business or industry, or the industry that you represent? Please explain your answer.

b) Very much

Question 36: Relative to the current regime as set out in the retained VABER, what would be the likely impact on your business's operations, or the operations of those you represent, if non-compete obligations that exceed 5 years in duration were no longer treated as 'excluded' restrictions? Please include examples and where possible, quantitative and/or qualitative evidence in your answer.

We believe the impact will be positive as explained in our response to Question 34 above.

Question 37: What are some of the benefits or efficiencies of non-compete obligations remaining exempt if the duration is less than 5 years? Please include examples and where possible, quantitative or qualitative evidence (or both) in your answer.

We do not think that there will be any such benefits or efficiencies created otherwise than in cases in which the supplier possesses significant market power, as per our response to Question 34 above.

Agency

Policy question

Question 38: The CMA invites views on the proposed recommendation[14] 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 CMA's views and proposed recommendation as we do not think that there are any material risks associated with agency that need to be reflected in specific new provisions of the UK VABEO. This is because, in the case of agency relationships, the supplier ultimately determines the commercial behaviour of the agent, hence the limited competition law risks involved in such situations. Of course, we would welcome guidance in this area as suggested by the CMA in the consultation document.

Environmental sustainability

Policy question

Question 39: The CMA invites views on the proposed recommendation [15] in respect of environmental sustainability and stakeholders to make any submissions they consider would help the CMA to develop useful guidance on this topic.

Impact questions

The CMA proposes that the Secretary of State does not make any changes to the UK VABEO in respect of environmental sustainability issues, but the CMA would instead seek to provide guidance on this topic in any CMA VABEO Guidance.

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.

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.

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

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14 Set out at paragraph 6.7. (see document)
15 Set out at paragraphs 6.10-6.12. (see document)

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.

Please see below our consolidated response which addressed Questions 39-42 together.

While we fully agree that environmental sustainability is an important public policy goal, we do not think that the CMA VABEO Guidance will be the right opportunity to provide guidance on how to incorporate sustainability goals into competition law assessment under the VABEO (or an Article 101(3) assessment). This is so for two reasons, as outlined below.

First, there has been very limited experience to date with the incorporation of environmental protection and sustainability goals into competition law analysis. Traditionally, competition law analysis has focused on the efficiency criteria set forth in Article 101(3). There are sound reasons for why non-competition goals have typically not been considered under Article 101(3). If, considering this background, the CMA were to use this consultation process to develop guidance on how to balance competition and sustainability concerns, the likely outcome would either be so general that it would in effect not assist market participants in the assessment of their agreements, or so prescriptive that it would not address situations that market participants may face in the future. Either way, legal certainty and predictability would not improve. In fact, such guidance may raise more questions than it would answer.

Second, incorporating sustainability goals into competition analysis is not an issue specific to agreements to be covered by the UK VABEO. It is at least equally relevant for competitor collaboration agreements and may even become an issue in licensing agreements. Thus, it does not appear to be justified to address this issue on this occasion.

Nevertheless, we recognise that there are legitimate expectations among market participants to have a better understanding of how they can enter into agreements pursuing sustainability goals in a competition law compliant way. We believe that a preferable approach at this point would be for the CMA, when consulted, to offer guidance to market participants about their specific agreements, and that the results of these consultations, and the principles developed therein, be made publicly available. Once competition enforcers and policy makers have been able to gather sufficient evidence that can inform their views and provide a reliable basis for any guidance they seek to provide, it would be the right opportunity to issue guidance on the incorporation of sustainability goals into Chapter I analysis in general.

Duration

Policy question

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

In our view, the suggested duration seems appropriate, especially since this is the first UK VABEO to be implemented, also in light of the dynamic and fast-paced UK market (also bearing in mind the constantly evolving e-commerce and digital platforms).

VABEO Obligation to provide information

Policy question

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

We agree with the CMA proposals here and we do not have any issues to raise at this stage.