Joint Working Party of the Bars and Law Societies of the United Kingdom ("JWP")[1]

Response to the BEIS technical consultation on the draft Vertical Agreements Block Exemption Order 2022

1. Introduction

1.1 The JWP welcomes the opportunity to respond to the Department for Business, Energy and Industrial Strategy's technical consultation on the draft Competition Act 1998 (Vertical Agreements Block Exemption) Order 2022 (the "draft VABEO").

1.2 The JWP notes that the draft VABEO follows the Competition and Markets Authority's ("CMA") recommendation to the Secretary of State to make a Block Exemption Order to replace the retained Vertical Agreements Block Exemption Regulation ("VABER"), once this expires in May 2022; a recommendation which the JWP supported.

1.3 We note also that the CMA Guidance which will accompany the draft VABEO has not yet been published by the CMA and this limits our ability meaningfully to comment on the draft VABEO. In general, the JWP considers that the focus of the CMA Guidance should be to take advantage of the flexibility afforded by the UK's departure from the EU to make meaningful changes that reflect UK policy objectives, and provide UK businesses with the greatest opportunity to design and operate their distribution systems in a way that meets their business needs. It is essential that the CMA Guidance provides clarity on the CMA's approach to the analysis of vertical agreements for the benefit of businesses and their legal advisors, so that the VABEO and Guidance provide a clear and genuinely broad safe harbour.

2. Specific issues

2.1 *Definition of "online intermediation service" ("OIS") (Article 2(1))*

2.2 In its Recommendations to the Secretary of State, the CMA proposed that providers of OIS should be treated as 'suppliers' for the purposes of the VABEO.

2.3 The draft VABEO has adopted this approach, specifying that "supplier" is defined as "*include[ing] an undertaking that provides online intermediation services irrespective of whether it is a party to the transaction it facilitates*". This definition suggests that providers of OIS, for example online travel agents, would cease to be categorized as 'buyers', even if they purchase products for resale in addition to providing OIS.

2.4 In such circumstances, the OIS providers that are also buyers would be denied the protection of the 'blacklist' of prohibited restrictions, with the consequence that pricing and marketing restrictions could be imposed on them by their suppliers, which would prevent them from providing pro-consumer benefits, such as discounts.

2.5 It is suggested that this outcome could be avoided if an amendment to Article 2 of the draft VABEO were introduced, amending the definition of a "buyer" as follows (the new text is in italics): "buyer" means the purchaser of the contract goods or services and includes an undertaking which, under an agreement to which the Chapter 1 prohibition applies, sells goods or services on behalf of another undertaking; *a supplier of OIS to a particular undertaking shall not cease to be a buyer in relation to such an undertaking in so far as it purchases goods or services from such an undertaking or sells goods or services on behalf of such an undertaking.*

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[1] The members of the Joint Working Party of the Bars and Law Societies of the United Kingdom on Competition Law comprise barristers, advocates and solicitors from all three UK jurisdictions; the membership includes both those in private practice and in-house. The JWP is co-chaired by George Peretz QC of Monckton Chambers (GPeretz@Mockton.com; tel 020 7405 7211) and Brian Sher, partner, CMS Cameron McKenna Nabarro Olswang LLP (brian.sher@cmscmno.com; tel 020 7524 6453).

2.6 ***Definition of "potential competitor" (Article 3(7))***

2.7 Article 1(1)(c) of the European Commission's draft revised Vertical Agreements Block Exemption Regulation includes a definition of "potential competitor" as meaning an undertaking that "*in the absence of the vertical agreement, would, on realistic grounds and not just as mere theoretical possibility, in case of a small by permanent increase in relative prices be likely to undertake, within a short period of time, the necessary additional investments or other necessary switching costs to enter the relevant market*".

2.8 The JWP considers that the wording "on realistic grounds and not just as a mere theoretical possibility" should also be included in the definition of "potential competitor" in Article 3(7) of the draft VABEO, as this wording is important to make clear that the prospect of entry must be real, rather than merely hypothetical.

2.9 ***Cross referencing error (Article 4(1))***

2.10 Article 4(1) of the draft VABEO refers to Article 3(4), this should be a reference to Article 3(3).

2.11 ***Treatment of RPM (Article 8(2)(a))***

2.12 In the JWP response to the CMA's consultation on its recommendation to the Secretary of State, the JWP respectfully disagreed with the CMA's proposed recommendation to continue to treat RPM as a hardcore restriction in the UK. The JWP continues to consider that this categorisation deters businesses from engaging in potentially efficiency-enhancing RPM, which could ultimately benefit consumers. Instead, we consider that RPM should be moved from a "by object" restriction to a "by effects" restriction in relation to UK activities. The US system has made this shift following Leegin and there has been no evidence that this has led to increased risk in competitive harm as a result.

2.13 We did, however, recognise that this would be a significant shift in the CMA's approach, and note that the position has not changed in the draft VABEO. The JWP therefore considers that there is definitely scope for clarification of the circumstances under which pro-competitive RPM can benefit from the exemption of section 9(1) of the Competition Act 1998, even if the CMA continues to treat RPM as a hardcore restriction. It would be very helpful for businesses in the UK to be able to rely on clear guidance on what can be acceptable, and we ask that this is included in the CMA's Guidance on the draft VABEO.

2.14 ***Calculation of turnover (Article 7(1))***

2.15 The JWP notes that the market share of the supplier is stated in Article 7(1) to be calculated on the basis of market sales value data "including sales to vertically integrated distributors". We assume that the inclusion of sales to vertically integrated distributors in the calculation should be applied across the market for the purposes of the application of the VABEO and not just to the calculation of the supplier's market share. This point could be clarified further by amending either to "including sales to all vertically integrated distributors"; or for greater clarity, to "including internal sales of all vertically integrated suppliers for the purposes of resale".

2.16 ***Geographic restrictions (Article 8(2)(b))***

2.17 The Explanatory Memorandum states that the territorial extent and application of the draft VABEO is the entirety of the UK. This implies that a ban on exports outside of the UK would not fall within the hardcore restrictions listed at Article 8. Given that this has been one of the most common legal questions arising in connection with the provision of competition law advice in relation to distribution arrangements since Brexit took effect, we consider it critical that the CMA Guidance expressly addresses this, rather than it being a matter of inference based on the draft VABEO language and the Explanatory Memorandum.

2.18 It is clear that the current lack of guidance - or even an informal position - from the CMA is leaving UK businesses in a position of significant uncertainty. We therefore urge the CMA

to include this point explicitly in its Guidance, similarly to the European Commission approach in paragraph 162 of its draft revised vertical guidelines.

2.19 The JWP considers that (i) the continued treatment of territorial and customer restrictions as hardcore restrictions and (ii) retaining the distinction between active and passive sales in the draft VABEO represents a missed opportunity for the UK to create a more flexible legal landscape for distribution in the UK consistent with genuine competition law principles.

2.20 We note that in the draft VABEO the approach taken to the UK is to make possible the carving up of the UK across a distribution network, potentially to quite small geographic areas. It would be helpful to clarify in the Guidance what is meant by a "geographic area". For example, it is intended that it would be possible to appoint a distributor to "North West London" and prevent active sales outside that "geographical area". In this regard we note that Article 8(5)(b) of the definition of "active sales" does not sit easily with the concept of sub-national territories, given that online media, price comparison tools and advertising on search engines are typically national in coverage. Based on the current definitions, the draft VABEO would appear to treat as an active sale the use by a sub-national distributor of any of these forms of online advertising.

2.21 ***Treatment of wide retail parity clauses (Article 8(2)(f))***

2.22 In its Recommendation to the Secretary of State, the CMA proposed that "*wide retail parity obligations are treated as a hardcore restriction under the UK Order*". As a consequence, these provisions would be treated as the most egregious form of restriction of competition law, which are blacklisted under the block exemption. This is different from the position that has been adopted by the European Commission in the draft VABER.

2.23 As noted in the JWP response to the CMA's consultation, some members of the JWP respectfully disagreed with this recommendation. Those members continue to hold this view. In the view of these dissenting members, there is insufficient evidence or experience to support the general inclusion of wide retail MFNs on the blacklist, particularly in international markets, where these provisions can play an important role in protecting UK consumers from upward price discrimination. Whilst in its Recommendations the CMA implicitly acknowledges that wide retail parity provisions may be pro-competitive (by maintaining that the parties to them are free to argue for an individual exemption, notwithstanding their inclusion on the blacklist of prohibited restrictions), UK businesses are highly unlikely to be willing to take the risk of using these provisions once they are added to the list of blacklisted restrictions.

2.24 ***Combination of distribution systems (Article 8(3)(c))***

2.25 Article 8(3)(c) refers to the "provision of greater protection" for members of selective distribution systems against sales from outside the geographical area to unauthorised distributors inside that geographical area. This is unclear and vague.

2.26 The JWP assumes the paragraph is meant to indicate that sales by distributors outside the area in which the selective distribution system operates to unauthorised distributors within that area can be prevented, which reflects the position taken by the European Commission in their draft revised VABER, but this should be clearly set out.

2.27 ***Definition of passive sales (Article 8(5))***

2.28 There is a lack of clarity in the drafting of the definition of passive sales in Article 8(5)(b). We assume that the paragraph is meant to mean that general advertising or promotion that reaches customers in other distributors' geographical areas or customer groups should be considered to be passive selling when it is a reasonable way to reach other customers including in the advertising distributor's own geographical area (which is made clear by the text after "for instance"), but the use of "outside those geographical areas" in line three causes confusion.

2.29 We suggest that the text is amended to read "…but which is a reasonable way to reach customers not in those other distributors' geographical areas or customer groups, for instance…"

2.30 ***Excluded restrictions (Article 10(1) and Article 11)***

2.31 Article 10(1) provides that a vertical agreement must not contain an excluded restriction. This formulation is not appropriate for excluded restrictions, which may be included in a vertical agreement, although they would not benefit from the block exemption. This is by contrast to hardcore restrictions, which remove the whole agreement from the protection of the block exemption.

2.32 Article 11 then refers to "cancelling the block exemption" which is not helpful or clear.

2.33 The JWP considers that it would be preferable to amend Article 10(1) to provide that an excluded restriction cannot benefit from the block exemption.

2.34 ***Obligation to provide information (Article 12)***

2.35 The JWP considers that a period of ten working days to provide information in connection with vertical agreements that the CMA may require is far too short; it takes time to locate and contact the right individuals in an organisation and gather relevant information, and we consider that a minimum period of 20 working days would be reasonable. There should also be provision for extensions to the period by agreement between the CMA and the relevant parties.

2.36 We assume that any such information gathering would be subject to the general information gathering provisions in the Enterprise Act 2002, but this should be made explicit on the face of the VABEO.

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On behalf of the JWP[2]

16 March 2022

[2] The authors would like to thank members of JWP for their contributions and Nicola Holmes for her assistance in the preparation of this submission.