

## Consultation on draft guidance to accompany the Vertical Agreements Block Exemption Order

### 1. Introduction

- 1.1 Freshfields Bruckhaus Deringer LLP welcomes the opportunity to respond to the Competition and Markets Authority (*CMA*)'s consultation on draft guidance (the *Guidance*) to accompany the new Vertical Agreements Block Exemption Order (*VABEO*).
- 1.2 This response is based on our significant experience and expertise in advising on issues raised by vertical agreements of many types, and, in particular, complex agency and exclusive and selective distribution arrangements. It is submitted on behalf of the Firm and does not represent the views of any of the Firm's clients, which comprise a wide range of companies, including distributors, manufacturers and suppliers of different sizes and with differing scopes of activity.
- 1.3 Likewise, this response does not necessarily in all respects represent the personal views of every partner in the Firm.

### 2. General

- 2.1 We strongly welcome the maintenance of the existing legal framework of a block exemption and detailed guidance, both for the legal certainty and cost-effective means of compliance they provide to businesses. We also welcome the many important clarifications and elaborations in the draft Guidance on the interpretation of the VABEO, and also on the application of Chapter I of the Competition Act 1998 (*CA98*) in situations falling *outside* the scope of the VABEO, especially in relation to the business models found in e-commerce and digital markets.
- 2.2 It is also helpful in relation to those aspects where there is convergence regarding the treatment of certain distribution arrangements as between the UK and the EU, that the Guidance tracks the language used in the draft Guidelines on Vertical Restraints (*DVGL*) that were published last year by the European Commission (*Commission*); as we have mentioned previously, consistency between the UK and EU approaches insofar as practicable is critical for businesses distributing goods and services in both the UK and the EEA (and particularly those with distribution networks covering both Northern Ireland and the Republic of Ireland).
- 2.3 Indeed, it is encouraging to see that the draft Guidance addresses a number of our previously highlighted concerns, providing further clarification and/or detail in respect of several areas of interest to our clients. For example:
  - in relation to permissible forms of information exchange in the context of dual distribution;
  - the treatment of fulfilment contracts and resale price maintenance;
  - the distinction between active and passive sales;

- the treatment of online sales and advertising bans; and
- further guidance on the relaxation of the restrictions relating to dual pricing and equivalence.

### 3. Areas where further Guidance is needed or where the draft Guidance needs to be clarified

3.1 There are, however, a number of areas where we consider the current draft Guidance to be deficient and where advisers and business would benefit from additional direction and/or clarification. We address each of these areas below.

#### *Dual distribution*

3.2 In its current form, there is nothing specific in the draft Guidance about how the definition of dual distribution applies to providers/platforms offering online intermediation services (*OIS*), other than a confirmatory statement that OIS providers are considered *suppliers* for the purpose of VABEO and cannot, therefore, be both a supplier and purchaser of services (paragraph 6.26 – on which see further below). Given that the Guidance seeks to provide certainty for businesses active in this area, greater clarity around the definition of dual distribution for the purposes of Article 3(5) of VABEO, in particular, as regards the treatment of OIS providers would be a welcome addition.

3.3 In addition, we maintain that it would be helpful if the Guidance were to contain some flexibility in indicating a reasonable interpretation of Article 3(5) VABEO so that the exemption remains applicable to agreements where any competing relationship at manufacturing level between the parties is marginal or not relevant (e.g., if it concerns products completely unrelated to the agreement, or if the distributor has a *de minimis* manufacturing presence thereby not affecting the vertical nature or “centre of gravity” of the agreement in question).

#### *Resale Price Maintenance*

3.4 Paragraph 8.20 of the Guidance, like its European counterpart, states that an agreement establishing minimum or fixed retail prices, which prevents the buyer from determining its resale prices independently, restricts competition *by object* within the meaning of Chapter I CA98. However, we believe that the Guidance should recognise that resale price maintenance (*RPM*) does not necessarily restrict competition by object. It may not do so, for example, if following an analysis of the relevant context, proven pro-competitive effects cast reasonable doubt on the conclusion that the agreement has a restrictive object (see e.g., *Budapest Bank*<sup>1</sup> and *Generics (UK)*<sup>2</sup>). Where a plausible efficiency rationale exists, the claimant is required to establish actual or likely restrictive effects before the parties can be required to justify their agreement under section 9 CA98.

3.5 While the Guidance acknowledges that RPM may lead to efficiencies, in particular when it is supplier driven, it would be helpful to receive further guidance in relation to this, in

---

<sup>1</sup> Case C-228/18, EU:C:2020:265.

<sup>2</sup> Case C-307/18, EU:C:2020:52.

addition to the points made in paragraph 8.22. For example, by listing the relevant assessment criteria as well as worked examples in which RPM does not raise competition law concerns and would therefore fall outside the Chapter I prohibition altogether.

- 3.6 Currently, there is limited explanation in the Guidance as to when RPM might be considered to be ‘indispensable’ to achieve established efficiencies, and how it can be demonstrated that consumers will receive a fair share of those benefits. We further note that while the Guidance contains two examples of arrangements involving RPM which might benefit from individual exemption in paragraph 8.22, the DVGL contain a third example in their equivalent section (namely paragraph 182(c)) in relation to how the extra margin provided by RPM may allow retailers to provide (additional) pre-sales services. There seems no underlying justification why this example is excluded from the Guidance and we would encourage this to be added.
- 3.7 Given the importance of recognising the potential pro-competitive benefits of RPM, in order to not deter potentially *pro-competitive* arrangements, it would be extremely helpful if the CMA would expand the Guidance on this topic by including examples of RPM practices which can still be pro-competitive on balance, and thus very unlikely to be susceptible to a successful challenge. More detailed and specific guidance, as well as any potential examples, would give businesses greater confidence in using the exemption.
- 3.8 Further, although the Guidance addresses the treatment of RPM in the case of *non*-true agents (paragraph 8.17), explicit acknowledgement of the legal position that RPM does not apply in circumstances where a *true* agency relationship has been established, would be a welcome addition to section 8 of the Guidance.
- 3.9 Finally, given that the draft VABEO does not consider OIS providers to be buyers in relation to the intermediated products, it stands to reason that when a supplier of an intermediated product sets a sale price on an online platform, it cannot be considered RPM within the meaning of Article 8(a) VABEO. We think this is the correct way of treating suppliers’ setting prices on its products when selling via online platforms. Acknowledging this interpretation of the VABEO will go a long way towards providing firms active in the online platform economy with legal certainty, which is the general purpose of the block exemption regulation.

#### *Fulfilment contracts*

- 3.10 We welcome the additional guidance provided on fulfilment contracts, which we note closely follows the text in DVGL. On the face of it, the Guidance appears to be limited to scenarios in which the supplier fixes a price with an end user. It is unclear, however, how the CMA would assess a scenario in which a supplier fixes a price with a party that is not an end user. We are not aware of any reasons why the assessment should be any different in such a scenario. If the CMA considered that the analysis should be limited to scenarios in which the customer was an end user, it would be helpful to make this point expressly later on in the paragraph, where the distinctions between a fulfilment contract and an agency arrangement are discussed.

### *Territorial restrictions*

- 3.11 The Guidance contains the same wording as the DVGL as regards the notion of “*shared exclusivity*” (see in particular paragraphs 8.69 and 10.59 of the Guidance and paragraph 102 of the DVGL). This is a welcome addition. However, the Guidance provides inadequate detail on this point and it remains unclear as to what the CMA would consider an acceptable number of distributors in such a situation, and what considerations companies and their advisers should have regard to when assessing a shared exclusive distribution system.
- 3.12 Separately, whilst we welcome the clarification in the Guidance that not *all* online advertising restrictions amount to hardcore restrictions, the Guidance would benefit from additional clarification about how it will apply in circumstances where there is one very significant provider of online advertising services in light of the additional point made in the Guidance that restrictions on the use of “*all most widely used advertising services in the respective online advertising channel*” would nevertheless give rise to a concern (paragraph 8.39). Given current advertising market dynamics, the scope and the flexibility being offered here is very uncertain.

### *Parity clauses*

- 3.13 We note that there is significantly more detail in the DVGL on the treatment of parity clauses, in particular, the structure of the analysis for determining whether such clauses – to the extent that they do not benefit from the block exemption – are likely to have anti-competitive effects and how any efficiencies resulting from the agreement in question can be weighed against identified restrictive effects under Article 101(3) Treaty on the Functioning of the European Union.
- 3.14 Accordingly, we would welcome the inclusion of similar specific guidance in respect of parity clauses used in agreements where the market share thresholds of the VABEO are exceeded. Similar to the DVGL, the Guidance could be further expanded to set out a structured analysis for: (i) determining whether parity obligations are in an individual case likely to have anti-competitive effects under section 2 CA98; (ii) determining whether parity obligations give rise to relevant efficiencies and pro-competitive benefits; and (iii) assessing how any identified restrictive effects are to be weighed against efficiencies and procompetitive benefits under section 9 CA98. In particular:
- (a) *In respect of (i)*, we consider that the Guidance should go further in emphasising the bespoke nature of many parity clauses, the terms and actual enforcement of which differ between companies and markets in which they operate. This would assist businesses in self-assessing whether or not a particular type of parity clause would be likely to produce anti-competitive effects. Further clarity could also be provided regarding the distinction between *retail* and *non-retail* parity obligations (see paragraphs 10.162 – 10.166) to provide more detail for businesses about the specific differences regarding how the regulator may approach assessing these two types of parity obligations; and

- (b) *In respect of (ii)*, the focus of the Guidance in relation to potential efficiencies is on free-riding only. The Guidance does not go into any additional detail about how parity clauses may be pro-competitive or benefit from efficiency justifications. To ensure an appropriate balance between considering anti-competitive effects and pro-competitive efficiencies it would assist business if the Guidance were to explain when efficiencies may arise. This could include, but is not limited, to: (i) platform credibility (the risk that without parity obligations suppliers could degrade the business of an intermediary); (ii) price transparency (with intermediaries allowing customers to compare prices); and (iii) encouraging distributors to concentrate their selling efforts on the suppliers' products, facilitating customer investment or market entry and/or reducing transaction costs.
- 3.15 It would also be useful if the Guidance could cover the assessment of parity obligations relating to *non-price* terms and the factors that may make wide retail parity obligations more or less problematic in a given context.

#### *Agency*

- 3.16 The Guidance is unsatisfactory in its current form, given that it excludes OIS providers from being classified as “agents”. The Guidance states that, “*in principle, platforms cannot qualify as agents*” (paragraph 4.19). The meaning of the qualification “in principle” is unclear, as it could indicate that there are exceptions to this rule, which reinforces the need for clarification in this important area.
- 3.17 Whilst the Guidance helpfully recognises that risk is the core factor in the identification of an agency relationship, the Guidance should clarify that platforms can - in certain circumstances - be genuine agents, in particular, where:
- (a) ownership of the products/services is not passed to the platform (the platform does not buy products from suppliers for resale);
  - (b) contracts concluded are formed between the supplier and customer; or
  - (c) the platform does not bear any of the risks related to the sale or provision of the goods or services, but receives a commission or remuneration for concluded contracts.
- 3.18 Indeed, we question the statement at paragraph 4.19 of the Guidance that OIS providers, as suppliers under Article 2(1) VABEO, cannot qualify as agents “*for the purpose of applying the Chapter I prohibition*”. This is legally incorrect. The question whether OIS providers may qualify as agents for the purpose of applying the Chapter I prohibition depends on the case law relating to Chapter I. Any undertaking – and there is no reason to exclude OIS providers – can be an agent if it fulfils the relevant criteria. The Guidance should instead, therefore, confirm that OIS providers can in certain circumstances be “genuine” agents. A case-by-case assessment is needed, and the Guidance should set out what the relevant factors are.

- 3.19 This would also be in line with the Commission’s decision in *E-books* which confirmed the possibility of concluding “genuine” agency agreements in an online environment with major online intermediaries such as Apple and Amazon.<sup>3</sup>
- 3.20 Moreover, the Guidance does not adequately explain why sellers cannot appoint OIS providers as their agents. The qualification that OIS providers are “suppliers” should not on its own be a valid distinguishing factor, because they supply online intermediation services just as traditional agents supply intermediation services.
- 3.21 Other justifications given in the Guidance (paragraphs 4.20 and 4.21) as to why OIS providers can never qualify as agents are unconvincing and, in any case, generally refer to issues of fact that should be considered on a case-by-case basis. For example:

*“Providers of online intermediation services generally act as independent economic operators and not as part of the undertakings of the sellers to which they provide online intermediation services”*

The fact that both entities are not part of the same undertaking is compatible with the “selling and purchasing function” of the contract goods or services forming part of the principal’s activities; this is consistent with the approach taken to date by the Commission and the EU Courts.

*“Strong network effects and other features of the online platform economy can contribute to a significant imbalance in the size and bargaining power of the contract parties and result in a situation where the conditions of sale of the contract goods or services and the commercial strategy are determined by the provider of online intermediation services rather than the sellers of the goods or services that are intermediated”*

The above statement, presented as justification for the exclusion, is inconsistent with the Commission’s decision in *E-books* (2012), which confirmed the possibility of concluding “genuine” agency agreements in an online environment with major online intermediaries such as Apple and Amazon.

*“...providers of online intermediation services often serve a very large number of sellers in parallel, which prevent them from effectively forming part of any of the sellers’ undertakings”.*

The current retained Guidelines on vertical restraints (paragraph 13) provide that “*it is not material for the assessment whether the agent acts for one or several principals*”; which is in line with the most recent EU court case-law. Those words do not appear in the draft Guidance, however.

*“[Providers of online intermediation services] typically make significant market-specific investments, for example in software, advertising and after-sales services, indicating that these undertakings bear significant financial or commercial risks*

---

<sup>3</sup> EC Memo, 13 December 2012, available at: [https://ec.europa.eu/commission/presscorner/detail/en/MEMO\\_12\\_983](https://ec.europa.eu/commission/presscorner/detail/en/MEMO_12_983).

*associated with the contracts negotiated on behalf of the sellers using their online intermediation services”*

The costs of designing and operating a website or software are equivalent to (and have the same legal significance as) more traditional businesses’ investments in premises/personnel (i.e. the basic costs of operating any business) and do not compromise the agency relationship (see also DVGL, paragraph 38). An online intermediary’s expenditure on advertising and search engine optimisation to attract consumers to its platform, which the intermediary is not contractually obliged to incur, are not “market specific investments” that compromise the agency relationship. EU Court case law provides that investments or activities that an intermediary undertakes at its own cost/risk may compromise its status as an agent only where those investments are “specifically required” in order to act for a principal or “*to the extent that the principal requires the agent to undertake such activities*”.

- 3.22 In so far as agency agreements involving online platforms do fall within the scope of the Chapter I prohibition, the Guidance should recognise that different principles to those governing other vertical agreements should apply where ownership of the products/services is not passed to the platform (there is no resale by the platform to the customer) and where the contracts are formed between the supplier and customer. In such cases, the platform is merely providing intermediation services and the principal should remain free to set its own prices. We note that a number of these points are addressed in detail in the draft EU Vertical Guidelines.

#### *Obligation to provide information*

- 3.23 Due to the severity of the consequences for non-compliance with the new obligation to provide the CMA with information, it would be helpful if the Guidance could expand upon what constitutes “*reasonable excuse*”.

#### *Extra-territorial application of the VABEO*

- 3.24 Finally, neither the VABEO nor the draft Guidance adequately addresses the CMA’s anticipated approach to, and enforcement priorities in respect of, jurisdiction and agreements incorporating restraints on selling outside of, or into, the UK. This is a fundamental omission in the Guidance and has important practical consequences for businesses operating within both the UK and the EEA. For example, it is unclear whether the CMA intends to follow an approach similar to that adopted by the Commission in the Vertical Block Exemption Regulation (*EU VABER*) and DVGL as regards trade within the EU, in that only restrictions on trade “in the UK” will be treated as hardcore under the VBAEO. Such an approach would suggest that contractual restrictions on sales from the EU into the UK would *not* infringe the Chapter I prohibition, except where there is a sufficient effect on UK trade.
- 3.25 We further note that the DVGL contain an explicit confirmation that the hardcore restrictions in Article 4 EU VABER apply to vertical agreements concerning trade within the EU, and that therefore, “*in so far as vertical agreements concern exports outside the Union or imports/re-imports from outside the Union, the case law of the CJEU suggests that such agreements cannot be regarded as having the object of appreciably restricting*

*competition within the Union or as being capable of affecting as such trade between Member States”* (paragraph 162). It would be helpful if the draft Guidance could be amended to include an equivalent confirmation with regard to exports outside the UK.

#### **4. Miscellaneous points**

- 4.1 There are a few instances in the Guidance where the CMA refers to restrictions of competition by object not being covered by the block exemption, which we believe should instead refer to “hardcore” restrictions (e.g. paragraphs 6.15 and 6.22). As these are two overlapping but different concepts further clarification would be welcome.

#### **5. Conclusion**

- 5.1 As mentioned, the Guidance addresses a number of important points set out in the VABEO, which will have a positive impact on those applying the new legislation and seeking to rely on the block exemption. However, there remain a number of aspects of the Guidance that could be further improved, either by including more detailed explanation and/or clarification or by supplementing with additional points not currently covered, but which are of practical importance for those applying the new rules. We would be very happy to discuss in further detail any of the points raised in this response.

**Freshfields Bruckhaus Deringer LLP**

**May 2022**