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NORTON ROSE FULBRIGHT

CMA consultation on draft guidance on the application of the Competition Act 1998 (Vertical Agreements Block Exemption) Order 2020

Norton Rose Fulbright LLP response

We welcome the opportunity to respond to the CMA's consultation, noting the importance for business of the EU and UK block exemptions for vertical agreements and detailed guidance regarding the same.

Norton Rose Fulbright has one of the largest antitrust and competition groups in the world, numbering around 200 lawyers across six continents. We have a large competition team in London, interacting with the CMA, the sector regulators, and the Competition Appeal Tribunal on a broad range of merger control, market and conduct investigations, appeals and litigation. A number of our team are former regulators, including several who have spent time within the CMA or its predecessor organisations.

We trust you will find our response helpful, and we would be very happy to discuss our views with you further.

We would like to highlight the following points:

- The CMA's draft guidance draws heavily on the European Commission's draft new Guidelines on Vertical Restraints, which we agree is a sensible approach. However, it is not always clear whether differences reflect intended divergence in substantive approach or have been made for another reason (e.g. brevity or readability). Given the number of businesses that need to ensure their vertical agreements comply with both UK and EU competition law, and the potentially significant implications of divergence on substance, it would be helpful if the CMA could identify places in the CMA's final guidance where it differs from the Commission's final new Guidelines, and also note whether such differences are substantive or, e.g. merely stylistic.

- We think the draft guidance could be clearer regarding the approach to assessing excluded restrictions where such restrictions are not capable of being severed from the agreement, including next steps after identifying that such a restriction cannot be severed. The draft guidance is clear as to the key principles and steps when assessing agreements containing hard-core restrictions and agreements containing excluded restrictions that are capable of being severed. However, it is less clear on the approach and next steps for agreements that contain excluded restrictions that are not capable of being severed, other than stating that such agreements are excluded from the benefit of the block exemption.

- There are a number of aspects of the draft guidance where statements or principles are made in relatively absolute terms, but there are areas of nuance that could alter the position and mean that potentially problematic restrictions are in fact pro-competitive. This includes aspects of the guidance concerning RPM and information exchange. We think reflecting these nuances in the guidance would be beneficial in terms of preventing any "chilling" of potentially beneficial arrangements.

- We think the guidance would benefit from greater and more consistent cross-referencing to help direct users to relevant parts of the guidance, recognising the length of the guidance and that users are unlikely to read the guidance from cover-to-cover. We appreciate that the CMA has been working under a compressed and challenging timeline to have its final guidance in place by 1 June 2022, and therefore may not have had sufficient time to complete details like cross-referencing prior to commencing its consultation. However, we consider this an important practical aspect that should be addressed before the guidance is finalised.

Please see below for further detail regarding our comments on the draft guidance.

1 Excluded restrictions

1.1 In addition to detailed guidance on specific types of restrictions, the draft guidance sets out key steps and principles in terms of the approach to assessing agreements containing hard-core restrictions (under Article 8(2)(a) to (f) draft Vertical Agreements Block Exemption Order (**VABEO**)) or excluded restrictions (under Article 10 VABEO). However, whereas the key steps/principles are clear regarding hard-core restrictions and also excluded restrictions that can be severed, we think the guidance would benefit from greater clarity regarding the approach where an agreement includes any excluded restrictions that are not severable.

1.2 Section 8 of the draft guidance explains that vertical agreements containing one or more of the hard-core restrictions listed in Article 8(2)(a) to (f) VABEO (which are generally "by object" restrictions) are excluded from the benefit of the block exemption, given such restrictions are presumed to harm competition. The draft guidance also explains that agreements containing such restrictions are generally likely to fall within the Chapter I prohibition and unlikely to fulfil the conditions for individual exemption under section 9(1) Competition Act 1998 (**CA98**) (although not every hard-core restriction necessarily falls within the Chapter I prohibition and parties may demonstrate efficiencies meeting the conditions of section 9(1)). These key principles are clear.

1.3 In relation to excluded restrictions under Article 10 VABEO, the draft guidance explains, at paragraph 9.2, that there is no presumption that such restrictions fall within the Chapter I prohibition or otherwise fail to fulfil the conditions for individual exemption under section 9(1) CA98. If any excluded restrictions are capable of being severed from the agreement the remainder of the agreement continues to benefit from the block exemption, and the excluded restrictions are subject to an individual assessment. Again, the general approach in this regard is clear.

1.4 Less clear from the draft guidance is the approach for agreements containing excluded restrictions that are not capable of being severed, other than that such agreements fall outside the benefit of the block exemption. The implication of this is that parties need to self -assess the entirety of such agreements. However, in practice, any such self-assessment would focus on the excluded restriction (i.e. just as it would if the excluded restriction could be severed). There are two possible outcomes of such an assessment:

(a) If the outcome is that the excluded restriction is unproblematic (either because it falls outside the Chapter I prohibition, or fulfils the conditions for individual exemption under section 9(1) CA98) this should mean the agreement as a whole is unproblematic (i.e. there is no need to assess the remainder of the agreement despite this technically falling outside the block exemption).

(b) If, to the contrary, the excluded restriction is deemed problematic after that assessment, the entire agreement would be problematic given the excluded restriction cannot be severed.

1.5 We think it would be helpful to clarify the approach in this regard in the guidance.

2 Territorial and language restrictions

2.1 We note that paragraph 2.16 of the draft guidance states that the VABEO does not apply to agreements implemented or intended to be implemented outside the UK. In that context, we understand that all references to territorial restrictions mean the UK or within the territory of the UK (i.e. the nations making up the UK or counties, cities, towns etc. within the UK) and do not mean restrictions regarding territories outside the UK. However, we think the guidance would benefit from making that point more explicitly.

2.2 Related to the above point, paragraph 10.11 sets out examples of possible reasons why vertical restraints may be justified, including at paragraph 10.11(c): "*where a supplier wishes to enter a new geographic market, for instance by expanding to provide products in another part of the UK, this may involve special sunk investments by the distributor to establish the brand on the market*". The equivalent wording in the European Commission's draft Guidelines on Vertical Restraints refers to "*for instance by exporting to another country*", such that the CMA's example appears to be narrower than the equivalent EU example, and as currently drafted would not cover suppliers providing contractual protections for UK-based distributors in respect of products which the supplier proposes to export to the UK for the first time. However, we do not believe that is the CMA's intention and therefore suggest that paragraph 10.11(c) be amended to state: "*for instance by newly exporting to the UK, or expanding to provide products in another part of the UK…*" [our additional text underlined].

2.3 With regard to languages, the definition of active sales in Article 8(5)(d) VABEO includes " *offering on a website language options different to the ones commonly used in the geographical area in which the distributor is established*". The CMA's draft guidance refers to that provision, as well as possible restrictions related to limiting the languages used on packaging or for the promotion of products. While we recognise that the CMA's guidance needs to refer to language differences (not least because of Article 8(5)(d) VABEO), language options and restrictions are naturally less likely to be relevant regarding UK vertical agreements than agreements concerning EU Member States assessed under

Article 101 TFEU and the Commission's Vertical Guidelines. We think it would be helpful for the CMA to acknowledge this point in its guidance, to avoid any (mistaken) inference that content regarding language restrictions has simply been copied from the Commission's Vertical Guidelines without appropriate consideration to whether/how such restrictions might apply in the UK context.

3 Agency agreements

3.1 We have the following comments regarding the section of the draft guidance that deals with agency agreements (paragraphs 4.8 to 4.30).

Market-specific investments

3.2 In relation to features of agency agreements, the CMA's draft guidance omits certain examples that are included in the Commission's Vertical Guidelines. Notably, in relation to not making market-specific investments in equipment, premises, training of personnel or advertising specific to the contract goods or services, the Commission's Guidelines include the following examples, but these are omitted from the CMA's draft guidance:

> "*such as for example the petrol storage tank in the case of petrol retailing, specific software to sell insurance policies in the case of insurance agents, or advertising relating to routes or destinations in the case of travel agents selling flights or hotel accommodation, unless these costs are fully reimbursed by the principal*"

3.3 In general, we consider that guidance is improved by including specific examples such as these. Moreover, the CMA's reasons for omitting these examples are unclear, including whether the CMA decided to omit them because it does not consider these to be good examples of agency arrangements and/or market-specific investments. We therefore think it would be helpful to include these examples in the CMA's guidance or to explain why they have been omitted (see further section 7 below).

Multiple agents

3.4 Paragraph 4.18(c) of the CMA's draft guidance states that where an agent acts for more than one principal this may indicate that the agent is independent and not an integral part of its principal's undertaking and, in particular, an agent is unlikely to be deemed integral if it acts on the same market for multiple competing principals. The CMA's approach in this regard differs to both the Commission's approach in its existing Vertical Guidelines (in which paragraph 13 states: *"…it is not material for the assessment whether the agent acts for one or several principals*"), and the Commission's draft new Vertical Guidelines which is silent on this point.

3.5 Contrary to the Commission's existing Vertical Guidelines, we are aware of EU case-law indicating that whether an agent acts for more than one principal is a relevant factor in the assessment of whether an arrangement amounts to agency for competition law purposes.[1] To the extent the CMA's position is based on such case-law we consider it would be helpful for the guidance to make this clear.

3.6 Paragraph 4.29 of the CMA's draft guidance highlights that agency agreements may facilitate collusion, for instance, where a number of principals use the same agents while collectively excluding other undertakings from using those agents, or if they use the agents to collude on marketing strategy or to exchange sensitive information. Given paragraph 4.29 refers to arrangements deemed to constitute agency for competition law purposes where agents are acting for multiple principals, this does not appear entirely consistent with paragraph 4.18(c), which states agency is unlikely in such circumstances. While we recognise paragraph 4.18(c) does not state there can never be agency for competition law purposes where an agent acts for multiple principals, we think it would be helpful for the guidance to clarify how paragraphs 4.18(c) and 4.29 fit together to avoid any possible confusion or perception of inconsistency in this regard.

[1] Case 311/85 – *Vereniging van Vlaamse Reisbureaus v Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten* [1987], EU:C:1987:418, paragraphs 20 to 21.

3.7 We note that the wording in paragraph 4.29 of the CMA's draft guidance is also included in the Commission's Vertical Guidelines (both its existing version and draft new version). This may therefore be an example where adopting a different approach to the Commission in one part of the CMA's guidance (i.e. paragraph 4.18(c)) requires a change to be made in another part of the guidance (paragraph 4.29), but which in this case has not been picked up.

Worked example of cost allocation for agency arrangements

3.8 Like the Commission's draft new Vertical Guidelines, the CMA's draft guidance (on pages 22 to 24) includes a worked example of how costs might be allocated for an arrangement to be categorised as agency for competition law purposes where a distributor also acts as agent for certain products for the same supplier. We welcome the use of examples such as this.

3.9 However, we think the worked example on pages 22 to 24 could be improved by using product names or types (even if made-up) that make it more obvious which products are within the same market, as opposed to referring to products A, B and C. This worked example is relatively long and would be easier to follow if product names/types were used in place of products A, B and C. This is a point we consider applies more generally regarding worked examples in published guidance, especially where such examples are relatively long.

4 Resale price maintenance (RPM)

4.1 We have three comments on paragraphs 8.10 to 8.26 regarding RPM, which we set out below.

Supplier request for a price increase

4.2 Our first comment regarding RPM concerns paragraph 8.11, which states that a restriction is clear-cut where a supplier requests a price increase and the buyer complies with such a request. We agree with this as a general principle, and note this is also stated in the Commission's draft new Guidelines. However, in a scenario where a buyer ignores or explicitly rejects such a request from a supplier, the buyer may subsequently wish to raise their prices for legitimate commercial reasons (e.g. because its costs have increased). It would therefore be helpful for the guidance to elaborate on the position of a buyer in such a scenario to clarify this and the types of evidence that could demonstrate any such future price increase by the buyer is not linked to the supplier's earlier request (e.g. passage of time since the request and the commercial rationale for the future increase).

Linking resale prices to those of competing products

4.3 Our second comment on RPM concerns paragraph 8.12(d), which provides that one of the indirect means by which RPM can be achieved is by linking a prescribed resale price to resale prices of competitors. We again recognise that the Commission's Guidelines contain the same statement. However, to the extent that resale prices are linked to the prices of competing products in a way that creates a maximum price this could be pro-competitive (e.g. "*price no higher than the price of [competitor product]*" or "*price at least [X] below the price of [competitor product]*"). We think the guidance could usefully add this clarification.

Possible efficiency defences

4.4 Our final comment on the sections of the guidance dealing with RPM concerns paragraph 8.22, which acknowledges that RPM may lead to efficiencies (in particular, where supplier driven), but that it is for the relevant parties to provide concrete evidence that the criteria set out in section 9(1) CA98 are met. Paragraph 8.22 includes two examples of such an efficiency defence, one concerning promotion of a new product and the other concerning a short-term low-price campaign.

4.5 We note that the CMA's efficiency defence examples regarding RPM are also included in the Commission's Guidelines, and that the Commission's Guidelines (both its existing version and draft new version) also include a third example – that in some situations, the extra margin provided by RPM may allow retailers to provide (additional) pre-sales services, in particular, in case of experience or complex products. It would be helpful to understand why the CMA has not included that third example in its

guidance, i.e. whether this is because the CMA does not believe this is a good example in the UK context or has excluded simply for reasons of brevity. See also section 7 below.

5 Restrictions of sales of spare parts

5.1 Paragraph 8.73 of the draft guidance explains the hard-core restriction set out in Article 8(2)(e) VABEO, i.e. the restriction, agreed between a supplier of components and a buyer who incorporates those components, of the supplier's ability to sell the components as spare parts to end- users or to repairers or other service providers not entrusted by the buyer with the repair or servicing of its goods.

5.2 The penultimate two sentences of paragraph 8.73 confirm that the agreement may place restrictions on supply of spare parts to repairers or service providers entrusted by the OEM with the repair or servicing of its own goods. This means that the OEM may require its own repair and service network to buy spare parts from itself or (if applicable) from other members of its selective distribution system. However, these sentences about permitted restrictions are followed by the following concluding statement that casts doubt on whether they are in fact permitted: "*The inclusion of such hardcore restriction in an agreement will have the effect of cancelling the block exemption…*"

5.3 We therefore suggest that the final sentence of paragraph 8.73 is amended to clarify that this does not refer to the preceding permitted restrictions, or that the current final sentence is moved so that it comes before the explanation of these permitted restrictions.

6 Information exchange

6.1 We welcome the guidance provided at paragraphs 10.170 to 10.179 of the draft guidance regarding information exchange in the context of dual distribution. One comment we would make regarding this part of the guidance concerns paragraph 10.176(a).

6.2 Paragraph 10.176(a) provides that information relating to the actual future prices at which the supplier or buyer will sell contract goods downstream is generally likely to restrict competition by object or otherwise is unlikely to be genuinely vertical. This is subject to the exception that an exchange of such information may be necessary to organise a coordinated short- term low price campaign consistent with the paragraph 8.22(b) of the draft guidance. This is also without prejudice to the possibility of exchanging information on the supplier's recommended resale prices or maximum prices. We agree with these principles.

6.3 A further appropriate exception we can envisage that is not currently mentioned in the draft guidance concerns a scenario where a supplier sets a maximum sale price but the buyer prices above that level (and may as a result be in breach of contract). In such a scenario, the supplier is likely to seek comfort from the buyer that they will reduce their price to comply with the maximum sale price. This would involve an exchange of information about the buyer's future price, with the aim of securing a lower price to the benefit of consumers. We think it would be helpful to amend the guidance to reflect that such an exchange may be permissible. The draft guidance recognises that information exchange is allowed regarding a supplier's maximum prices, but our reading is that this means only in respect of information from the supplier about their maximum prices.

7 Ease of use of the guidance

7.1 We welcome detailed published guidance, noting that the draft guidance exceeds 140 pages. However, the longer any guidance, the greater the importance of steps to make such guidance as user friendly as possible. As explained below, we believe there are two relatively simple steps that would considerably improve ease of use of the guidance.

Comparison with EU guidance

7.2 The draft guidance draws heavily on the Commission's equivalent Vertical Guidelines, and we agree with that approach. Given that many businesses will need to assess their vertical agreements for compliance with both EU and UK competition law and the potentially significant implications of divergence on substance, it would be helpful for the CMA to publish a document comparing its final

guidance against the Commission's final revised Vertical Guidelines, and to provide commentary on differences between its final guidance and the Commission's final new Vertical Guidelines, in particular to highlight where differences reflect substantive divergence.

7.3 In our response, we have mentioned certain parts of the draft guidance (but not every part) where the CMA's drafting is similar but not identical to the Commission's Guidelines. We recognise there are a number of good reasons why the CMA may not always want to replicate the exact content of the Commission's Guidelines, including for clarity, readability, brevity, or (more crucially) because a different substantive approach is appropriate in the UK context. However, it is not always obvious why the CMA has, e.g. omitted certain text or a specific example, or adopted similar but different wording to the Commission. A commentary document that categorises any differences would therefore be helpful.[2]

Cross-referencing

7.4 To the extent that the same issues or types of restrictions are dealt with in different parts of the CMA's guidance, it would be helpful to include greater cross-referencing to direct users of the guidance to the relevant parts. This is particularly important given users will not generally read the guidance cover-to-cover and will instead focus on particular sections of greatest relevance to the agreement they are analysing.

7.5 We recognise that the draft guidance includes some cross-referencing, but not always in a complete or consistent way. For example, regarding agency agreements, paragraph 4.28 refers to post-term non-compete provisions and cross-refers to further guidance provided in paragraphs 9.7 and 10.37 to 10.56. However, paragraph 9.7 (which explains the excluded restriction under Article 10(2)(b) VABEO, i.e. a post-term non-compete) does not direct users of the guidance to any other paragraphs for further guidance, and (despite the cross-referencing in paragraph 4.28) paragraphs 10.37 to 10.56 do not refer to paragraphs 4.28 or 9.7.

7.6 There are also sections of the draft guidance that are related, but contain no cross- referencing at the moment. For example, paragraph 9.8 of the draft guidance explains the reason for the excluded restriction in Article 10(2)(c) VABEO (any direct or indirect obligation causing members of a selective distribution system not to sell the brands of particular competing suppliers), but does not refer readers to paragraphs 10.101 and 10.102 where Article 10(2)(c) is expressly mentioned and the approach regarding this type of restriction considered further. Similarly, paragraphs 9.4 to 9.6 explain why non-compete obligations that exceed five years or are indefinite are excluded restrictions under Article 10(2)(a) VABEO, but do not refer users of the guidance to section 10 where single branding is covered.

8 Expected duration of the guidance

8.1 The European Commission's general approach is not to revise its Guidelines related to the EU Block Exemption Regulations until a Block Exemption Regulation expires and is replaced by a new version, with revised Guidelines accompanying that new version.

8.2 It would be helpful to know whether the CMA intends to adopt the same approach as the Commission, i.e. whether the CMA's published vertical guidance that applies from 1 June 2022 will remain unchanged until the VABEO expires (or is extended or replaced) on 1 June 2028, or the CMA might revise its vertical guidance (if appropriate) before 1 June 2028.

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[2] Any such commentary document could be relatively simple, e.g. using colour-coding to categorise types of differences and further explanation only needed if differences relate to substantive approach.