Response to the CMA's consultation on draft guidance on the application of the Chapter I prohibition in the Competition Act 1998 to horizontal agreements

Introduction

Dentons welcomes this opportunity to provide its views on the draft Guidance on the application of the Chapter I prohibition in the Competition Act 1998 to horizontal agreements ("the Horizontal Guidelines").

The Horizontal Guidelines provide essential guidance. They can, however, be improved, particularly considering the changing economic dynamics since their publication, as well as the CMA's and stakeholders' experiences in their application. Taking into account specific features of the UK economy in the review is welcomed. However, it is also important to keep to a minimum any differences between the UK and the EU, given international businesses' general preference for consistency.

Dentons regularly advises UK and international clients on horizontal agreements and practices affecting UK markets. Therefore, our response to this consultation is informed by our experience of advising clients on these issues.

We would be pleased to discuss any part of our response further with the CMA.

We have followed the structure of the CMA Consultation document to provide our responses.

Executive Summary

1 Joint ventures

1.1 Paragraphs 3.8 - 3.10 are a welcome attempt to clarify the application of competition law to agreements between parent(s) and the joint venture, which is an issue of significant importance for businesses, in the face of case law from the Court of Justice of the EU which has not always been easy to reconcile.

1.2 However, there are a number of ways in which the guidance could be clarified or expanded:

1.2.1 It is not clear if Paragraph 3.8 is supposed to be valid for both the ex-post imputation of liability and the ex-ante structuring and assessment of joint ventures. For example, the guidance states that "in the context of agreements between parents and their joint venture, when it is demonstrated that the parents **exercised** decisive influence over the joint venture, the CMA will typically not apply the Chapter prohibition…" [emphasis added]. This suggests that it applies to an ex-post analysis only, although we presume that is not the CMA's intention given the guidance is intended to allow businesses to self-assess the implications of commercial arrangements under competition law in advance. It would be helpful if the CMA could clarify this point. We suggest that the guidance make clear that, under UK competition law, the same principles apply for the purposes of the assessing the competition law implications of a joint venture when it is being created as apply when the CMA considers the

liability of parent(s) and joint ventures for competition law infringements (or if they do not that the different considerations are explained).

1.2.2 The wording above also refers to "decisive influence", which the CMA has, based on EU case-law, used to determine liability for breach of competition law by a parent (including parents of joint ventures). Where the parent has less than 100% of shares of the subsidiary or joint venture entity, the CMA has looked at economic, organisational and legal links which tie the subsidiary to the parent company, and show that the parent was in a position to exercise decisive influence over the subsidiary and that it actually did so. The CMA could explain what would be required to meet the decisive influence test on a forward-looking basis, given that the actual exercise of such decisive influence, such as voting patterns etc, is considered in cases involving the imputation of liability. Is it the case that the power to exercise decisive influence is sufficient, but that in attribution of liability cases actual exercise of those powers is required?

1.2.3 Generally, it would be helpful if the principles outlined in the guidance could be illustrated by an example, or by reference to typical clauses which might be permissible between a parent and a joint venture which are considered to be part of the same undertaking (e.g. a non-compete obligation on the parent relating the scope of the joint venture's activities or sharing of CSI relating to the JV's activities) and those which would be regarded as between separate undertakings and to which competition law would apply (e.g. a non-compete obligation on the joint venture not to compete with the parent outside the scope of the joint venture).

2 Research and development agreements

2.1 Clarification of the 'primary object' concept in Article 3(3) of the R&D Block Exemption Order (BEO) – paras 4.53 - 4.55 of the Draft Horizontal Guidance

2.1.1 Article 3(3) of the R&D BEO provides that R&D agreements stipulating the assignment or licensing of IPRs (i.e. technology transfer) would benefit from the R&D BEO if the technology transfer provisions (a) do not constitute **the primary object** of the R&D agreement and (b) are directly related to and necessary for the implementation of the R&D agreement. Although the 'primary object' concept is not new, in practice, it is not always easy to make this assessment, so the Draft Horizontal Guidance could provide further clarification. For example, there are circumstances (in particular, in the pharma sector) where one of the parties to the R&D agreement license its patented technology to the other party at the outset of the R&D project, and then they jointly continue to develop this proprietary technology. It would be good to see further explanation as to whether such cases would fall under Article 3(3) of the R&D BEO in the Draft Horizontal Guidance.

2.2 Clarification as to Article 5(3)(c) of the R&D BEO – para 4.61 for the Draft Horizontal Guidance

2.2.1 Access to the final results for the purposes of (i) further R&D and (ii) exploitation of the results is one of the conditions of the R&D BEO. However, as per Article 5(3)(c) of the R&D BEO, an

agreement can still benefit from the block exemption, if access to the final results for the purposes of exploitation is limited where the parties limit their rights of exploitation in accordance with the R&D BEO (e.g. specialisation relating to exploitation, see para 4.50 of the Draft Horizontal Guidance). For avoidance of doubt, it would be beneficial to add a sentence to para 4.61 of the Draft Horizontal Guidance to clarify that Article 5(3)(c) of the R&D BEO relates to limiting access to the final results for the purposes of *exploitation of the results*, so the agreement must still provide for all the parties to have access to the final results for the purposes of *further R&D*.

2.3 The new test for undertakings competing in innovation

2.3.1 Compared to the test for not competing undertakings, the new test would make it more difficult for undertakings competing in innovation to benefit from the R&D BEO, and considering the lack of case law, it the CMA may consider publishing a guidance on the application of the new test in particular considering stakeholders' concerns and questions. Given that the application of the new test would require case-by-case analysis, such guidance could support stakeholders by further elaborating on the new concepts (e.g. competing R&D efforts) and providing examples similar to the one in pages 72-74 of the Draft Horizontal Guidance. Further guidance as to the assessment of R&D agreements between undertakings competing in innovation under Chapter 9 of the Competition Act 1998 would also be helpful.

2.3.2 It would be beneficial to explain further under which circumstances R&D clusters would be considered to have 'substantially the same aim or objective' in para 4.96 of the Draft Horizontal Guidance.

2.3.3 It is unclear how the parties to the R&D agreement will be able to assess the comparability of competing R&D efforts on the basis of reliable information in practice as this requires, at least to a certain extent, having insights into the third parties' existing projects, resources and operations. For example, while it may be easier for the parties to the R&D agreement to gather information regarding big (public) companies' projects and resources, the same may not be true if they want to access information on the activities and resources of start-ups and private companies. Even where the parties to the R&D agreement have some information about competing R&D efforts, this would probably be far from sufficient in detail to form the basis for reliable information. Therefore, further practical guidance on how the CMA envisages the parties to back up their assessment and the evidence threshold would be welcome.

2.3.4 Article 8(5)(b) (i.e. identifying sufficient third parties who have the ability to engage independently in relevant similar R&D efforts) aims to make it easier for the parties to the R&D agreement to benefit from the block exemption even when they could not identify third parties who are already engaging in 'competing R&D efforts'. However, in practice and considering the elements listed in Article 9(3)(b) of the R&D BEO and para 4.105 of the Draft Horizontal Guidance, this may not be easy as again it requires the parties to have insights regarding third parties' resources and operations. Thus, the CMA may assist stakeholder by providing further practical guidance.

2.3.5 On a related point, para 4.105(e)(iv) of the Draft Horizontal Guidance refers to 'low barriers to entry' as evidence supporting the assessment that there are third parties who are able independently to engage in competing R&D efforts. It would be helpful if the CMA could explain what is meant by 'low barriers to entry' (e.g. no proprietary technology that needs to be licensed to engage in a competing R&D effort) in this particular context.

3 Product agreements

3.1 Paragraph 5.4 to 5.6 refer to agreements relating to the production of a "product". Footnote 13 of the Draft Guidance states "*In this Guidance, goods, services and technologies will be referred to collectively as 'products', unless the context suggests otherwise*". It would be useful refer to this footnote here and widen the definition to include "product" (not only "products" – plural).

3.2 Para 5.4 defines horizontal subcontracting as agreements "concluded between undertakings operating in the same product market as regards the product or products that are the subject of the agreement irrespective of whether they are actual or potential competitors". In this regard:

(a) Footnote 207 defines vertical subcontracting as subcontracting between companies "operating at different levels of the market", which is not the same delimitation criterion. It would be helpful to outline whether the CMA purposefully makes this distinction.

(b) We flag that the definition "operating at the same product market" could capture subcontracting agreements between integrated manufacturers operating in different geographic markets, even where (i) they are not potential entrants into each other´s geographic market, and (ii) they are companies operating at "different levels of trade" (e.g., a supermarket chain and a white label pasta manufacturer).

3.3 Paragraph 5.41 states that "in some industries where production is the main economic activity", even a "pure production agreement" can itself limit competition. It would be helpful to clarify how to identify an industry where production is the main economic activity. Similarly, it would be helpful to specify what a "pure production agreement" means.

4 Purchasing agreements

4.1 Definition of joint purchasing arrangements

Paragraph 6.2 helpfully clarifies that a joint purchasing arrangement may also involve additional activities including joint distribution, quality control and warehousing, to avoid duplication of delivery costs. The implication is that an arrangement which involves such additional activities will still be considered a joint purchasing arrangement where joint negotiations and/or purchasing is the focus of the arrangement, but it would be helpful to state this explicitly.

4.2 Distinction between joint purchasing arrangements and buyer cartels

4.2.1 We welcome the distinction between genuine joint purchasing arrangements and buyer cartels in paragraphs 6.8 – 6.16 (inclusive). To further clarify this distinction, we suggest amending the second sentence of Paragraph 6.10 to refer to "*genuine* joint purchasing arrangements" rather than "*other* forms of joint purchasing arrangements" (italics added for emphasis).

4.2.2 We suggest moving Footnote 255 from the end of Paragraph 6.12 to the end of Paragraph 6.13(a), as it relates more closely to the latter.

4.2.3 Paragraph 6.13(a) places a great deal of importance on suppliers' knowledge of a joint purchasing arrangements in determining whether it is a buyer cartel, which we are not completely convinced by. We think it would be useful to explicitly clarify that a supplier not being aware of a joint purchasing arrangement is not in itself sufficient to characterise the arrangement as a buyer cartel.

4.2.4 We do not agree with the final sentence of Paragraph 6.13(a) which states that a supplier learning about a joint purchasing arrangement indirectly is not likely to be sufficient to show that the joint purchasing arrangement has been made clear to the supplier. In our view, it should be sufficient that a supplier has knowledge of the joint purchasing arrangement, whether through direct or indirect means.

4.2.5 Whilst we agree with Paragraph 6.13(b) that the existence of a written agreement may help undertakings to assess whether their arrangement amounts to a buyer cartel, it would be helpful clarification if the CMA were to explicitly state that an arrangement is not necessarily a buyer cartel where there is no written agreement.

5 Commercialisation agreements

5.1 Paragraph 7.20 discusses reciprocal commercialisation agreements. On the one hand, if such an agreement is objectively necessary to enter each other's market, it is unlikely to create horizontal concerns. On the other, if the agreement reduces the decision-making independence of one or more of the parties with regard to entering the other parties' market by limiting its incentives to do so, it is likely to give rise to restrictive effects on competition. We assume that the latter scenario would arise as a result of long term, exclusive arrangements, for instance, but it would be helpful if that was specified along with any other typical incentive-reducing factors.

5.2 At various points distribution agreements between competitors are discussed, which is helpful as these are relatively common. However, we note that information exchange between the parties to such an agreement is not dealt with in any detail.

5.3 At Paragraph 7.23 there is a recognition that some degree of information exchange is required to implement a joint commercialisation agreement. Reference is also made to the

separate section on information exchange to aid analysis. However, that information exchange section is not explicit in relation to the information which might be acceptable in the context of distribution between competitors. In the same way as the CMA has done in the VABEO Guidance for dual distribution at Paragraph 6.25 it would be helpful for the CMA to be clearer about the type of information which might be regarded as necessary for the implementation of the agreement or, alternatively if the assumption that all competitively sensitive information has the potential to cause concerns, the manner in which such information must be shared in order to avoid such concerns.

5.4 We assume, for example, that the CMA would consider that a supplier sharing information in advance about future increases to the price that the distributor will pay (or increases to the supplier's RRP) could have restrictive effects, as it may influence the distributor's own pricing decisions as regards its own competing products. However, this information is also often necessary for the implementation of the agreement, in order for the distributor to prepare for price increases. We understand the guidance to mean that even where information is required, that does not mean no competition concerns arise. Rather, the competition risks can be managed by information barriers at the distributor to ensure that its commercial / pricing team does not have access to that information. However, this could be clearer.

5.5 The new section of the joint bidding section is a good addition to the guidance. We note that where the tender provides for separate lots, parties that are able to bid for one or more lots will be regarded as competitors for the whole contract. We assume that this stance is limited to considering effects on the competition for the tendered contract. It should not impinge on the parties' ability to share information where the bidding consortium parties do not actually compete in relation to all of the tender requirements. For example, there is no reason why a joint venture party which can provide only one aspect of the tenderer's requirements (e.g. logistics which forms a separate lot) should not receive pricing information about products provided for in other lots when preparing the bid. However, if the parties compete in relation to logistics, information barriers may be required. Generally, since information barriers can be a key part of consortia bidding, further guidance (and an example which discusses management of information exchange risks) on this aspect would be welcomed.

5.6 We note that the CMA has removed the example from previous guidance which discussed a no-poach clause in the context of sub-contracting. Given the additional guidance on joint bidding, which might often involve sub-contracting and no-poach clauses (if the joint bid is designed to expand capacity for example), retaining that example, or building in the analysis of a no-poach agreement into another example would be welcome.

6 Information exchange

6.1 We welcome the references made to big data analytics and machine learning in para 8.2. It would be helpful if further guidance is given specifically with these technological advances in mind.

6.2 At Paragraph 8.53, the guidance states that "*when an undertaking receives competitively sensitive information from a competitor (be it in a meeting, by phone, electronically or as input in an algorithmic tool), it will be presumed to take account of such information and adapt its market conduct accordingly* ***unless it responds with a clear statement that it does not wish to receive such information*** *or reports it to the administrative authorities.*" This is an important point. One reading of that might be that rejecting the information is always sufficient to escape liability for a breach of Chapter I. It would be better if the guidance more explicitly addressed the fact that there may be situations where rejection / public distancing is not enough, because the individual cannot "unknow" the unsolicited information received. For example, depending on the role of an individual, there may be situations where the recipient is effectively ruled offside from commercial decision-making for a period of time. Businesses need to understand the CMA's approach to such scenarios, so that they can assess whether (and how) the risk can be fully mitigated (and what evidence they would need to furnish to the CMA in relation to the safeguards taken should the matter subsequently be investigated).

6.3 Para 8.51 explains that a concerted practice may be formed by "introducing a pricing rule in a shared algorithmic tool". This language should be further refined to ensure that the fundamental distinction between unilateral and collusive conduct is not blurred. An algorithm may be shared by competitors without their knowledge (e.g. if Company A is using (unknowingly) a price monitoring algorithm sourced from a software developer X that is also used by competitor B).

6.4 Para 8.59(a) describes the "hub" in a hub-and-spoke arrangement as "a common supplier or manufacturer". Information exchange through "common agency" are deal with at para 8.59(c), as also being able to facilitate exchanges between its members". This pre-supposes that the two competitors engaging in information exchange must be members. Does the CMA envisage a situation where information is exchanged through a third party with who the competitors do not have contractual relations, and/or are not members? If so, this should be included.

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