LIDC

LIGUE INTERNATIONALE DU DROIT DE LA CONCURRENCE
INTERNATIONAL LEAGUE OF COMPETITION LAW
INTERNATIONALE LIGA FÜR WETTBEWERBSRECHT

Questions for National Reporters of LIDC BORDEAUX 2010

Question A: Which, if any, agreements, practices or information exchanges about prices should be prohibited in vertical relationships?

UK National Reporter: Bruce Kilpatrick, Addleshaw Goddard

1. Legal framework

1.1 What is the legal framework in the national competition act applicable to vertical agreements, i.e. are these agreements in generally permissible or in part impermissible. Are vertical agreements or some of them illegal per se, presumed illegal or assessed on the basis of a type of rule of reason analysis? Does a block exemption apply to vertical agreements in your jurisdiction?

Introduction

1 The two main substantive provisions which may be applied to vertical agreements in the United Kingdom (**UK**) are Article 101 of the Treaty on the Functioning of the European Union (**TFEU**) and section 2(1) of the Competition Act 1998 (**Competition Act**) (the **Chapter I prohibition**).

2 The Chapter I prohibition is modelled on Article 101 TFEU and prohibits agreements between undertakings that may affect trade in the UK and which have the object or effect of restricting competition within the UK or a part of the UK. Section 60 of the Competition Act requires the OFT and UK courts, in so far as possible, to deal with questions arising in relation to the Chapter I prohibition in a manner consistent with the treatment of corresponding questions arising under EU law. Hence, the legal framework in the UK is intended to ensure that the substantive assessment under the Chapter I prohibition dovetails with Article 101 TFEU. As indicated below, any differences between the assessment of vertical agreements under UK competition law, on the one hand, and EU competition law, on the other, have been gradually eroded over time.

The Chapter I Prohibition

3 Section 9(1) of the Competition Act mirrors Article 101(3) TFEU so that an agreement which falls within the Chapter I prohibition but which satisfies the conditions set out in section 9(1) is not prohibited. The wording of section 9(1) essentially reflects that of Article 101(3) except that in the first condition the phrase "*of goods*" has been omitted. This is intended to make clear (consistent with the practice of the European Commission) in relation to Article 101(3)

that improvements in production or distribution in relation to services may also satisfy the first condition in section 9(1).[1]

4 Like the approach under European law, the UK competition authorities recognise that vertical agreements do not generally give rise to competition concerns in that, although they may hinder intra-brand competition, they can stimulate inter-brand competition and thereby provide benefits to consumers. The Office of Fair Trading (**OFT)** has indicated in its Guidance on Vertical Agreements (**OFT 419**) that vertical agreements do not generally give rise to competition concerns unless one or more of the parties to the agreement possesses market power on the relevant market, or the agreement forms part of a network of similar agreements.[2]

5 Indeed, historically in the UK, vertical agreements were excluded from the ambit of the Chapter I prohibition altogether, under the Land and Vertical Agreements Exclusion Order 2000[3] (**Exclusion Order**) which was issued by the Secretary of State for Trade and Industry in 2000 under section 50 of the Competition Act.[4] The Exclusion Order did not, however, preclude the application of Article 101 where there was an effect on trade between EU Member States. Equally, it did not prevent the application of Article 102 and/or the Chapter II prohibition (the UK's equivalent of Article 102 TFEU).

6 The Exclusion Order was not subject to a market share test such as that which applies under the Vertical Agreements Block Exemption[5] (**VABE**) and only contained one "hardcore" restriction, which related to price-fixing. An agreement which included a price-fixing restriction could not therefore benefit from the exclusion. As is the case with VABE, the OFT could withdraw the benefit of the exclusion in certain cases.

7 The Exclusion Order was revoked by the UK Government in 2004 by the Land Agreements Exclusion and Revocation Order[6] so as to remove vertical agreements from its scope, with effect from 1 May 2005.[7] This was to avoid two different sets of competition rules applying to vertical agreements when the modernisation of EU competition law took effect.

8 Since the modernisation of EU competition law on 1 May 2004, the OFT and the UK courts have been able to apply and enforce Articles 101 and 102 of the TFEU as well as national competition law when national competition law is applied to agreements which may affect trade between Member States or to an abuse prohibited by Article 102 TFEU.

Parallel Exemptions and the Vertical Agreements Block Exemption

[1] The OFT has regard to the European Commission's Notice *Guidelines on the Application of Article 81(3) of the Treaty* (OJ C101 27.04.2004, p97) when considering the application of Article 101(3) TFEU and section 9(1) of the Competition Act.

[2] OFT Competition Law Guide on *Vertical Agreements* (OFT 419, Edition 12/04), paragraph 7.4.

[3] SI 2000 No 310.

[4] Section 50 of the Competition Act grants the Secretary of State the power to make orders excluding vertical agreements from the Chapter I prohibition and/or the Chapter II prohibition (the UK's equivalent of Article 102 TFEU) in the Competition Act.

[5] Commission Regulation (EC) No 2790/99, OJ [1999] L 336/21, 29.12.1999.

[6] Competition Act 1998 (Land Agreements Exclusion and Revocation Order) SI 2004/1260.

[7] The Land Agreements Exclusion Order continued to provide an exclusion from the Chapter I prohibition (although not Article 101 of the TFEU) in respect of land agreements. An exclusion therefore still exists in the UK in respect of "land agreements." However, this exclusion will be repealed as of 6 April 2011.

9 Section 10 of the Competition Act provides that an agreement is exempt from the Chapter I prohibition if it is covered by a finding of inapplicability by the European Commission or an EU block exemption regulation, or would be covered by an EU block exemption regulation if the agreement had an effect on trade between EU Member States.[8]

10 Section 10 therefore has the effect of exempting vertical agreements from the application of the Chapter I prohibition where those agreements fall within the terms of VABE. Agreements falling within VABE will be exempt from the application of both Article 101(1) of the TFEU and the Chapter I prohibition. The OFT has regard to the European Commission's Guidelines on Vertical Restraints[9] in its assessment of vertical agreements in relation to both Article 101 and the Chapter I prohibition.

11 The OFT (but not the UK courts) has the power under Article 29(2) of the Modernisation Regulation[10] to withdraw the benefit of VABE from any agreement where:

- the agreement in question has effects that are incompatible with Article 101(3) in the territory of the UK, or a part of the UK; and
- the relevant territory has all the characteristics of a distinct geographical market.

12 If the OFT decides to withdraw the benefit of VABE from a particular agreement, at the same time it establishes that the agreement infringes Article 101. The finding of infringement will, however, only have effect from the date of the withdrawal. Withdrawal of VABE will also have the effect that any parallel exemption will cease to have effect by virtue of section 10(4)(b) of the Competition Act.

13 Vertical agreements where the market share threshold in VABE is exceeded will be assessed under Article 101 and/or the Chapter I prohibition. Of course, it is possible that, even if such an agreement is found to restrict competition within the meaning of Article 101(1) and/or the Chapter I prohibition, it may nevertheless satisfy the conditions in Article 101(3) and/or section 9(1) of the Competition Act.

Article 102 TFEU and section 18(1) Competition Act

14 Where an undertaking which holds a dominant position in a market enters into a vertical agreement, that agreement may be subject to Article 102 and/or section 18(1) of the Competition Act (the **Chapter II prohibition**). The Chapter II prohibition prohibits an abuse by one or more undertakings of a dominant position within the UK, or any part of it, which may affect trade in the UK. By virtue of the Modernisation Regulation, Article 102 may also be applied in parallel by the UK competition authorities and courts where there is an effect on trade between EU Member States. Section 60 of the Competition Act requires the OFT and UK courts, in so far as possible, to deal with questions arising in relation to the Chapter II

[8] Where an agreement would be covered by an EU block exemption regulation if it had an effect on trade between Member States the OFT has the power to impose conditions on the parallel exemption or cancel the exemption if the agreement has effects in the United Kingdom, or a part of it, which are incompatible with the conditions in section 9(1) of the Competition Act.

[9] Guidelines on Vertical Restraints [2000] O.J. C291/1

[10] Council Regulation of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (1/2003/EC).

prohibition in a manner consistent with the treatment of corresponding questions arising under EU law.

Market studies and investigations under the Enterprise Act 2002

15 Finally, the OFT has the power under the Enterprise Act 2002 (the **Enterprise Act**) to refer a market to the Competition Commission for investigation where it has reasonable grounds for suspecting that any features of a market in the UK for goods or services prevent, restrict or distort competition in connection with the supply or acquisition of any goods or services in all or part of the UK.[11] The Competition Commission has up to two years to issue its final report. If it concludes that there are adverse effects on competition it must decide what, if any, action it or a third party should take to remedy them.[12]

16 Market investigations may, in certain circumstances, be relevant for dealing with possible competition concerns in relation to vertical agreements. For example, the OFT referred the market for the supply of groceries to the Competition Commission in May 2006, as a result of concerns relating to the planning regime, practices connected to land (such as the use of restrictive covenants) and the buyer power of the major supermarkets. The Competition Commission concluded (following a two year inquiry) that high concentration levels and the control of land had an adverse effect on competition in certain local markets for the supply of groceries. It also concluded that the exercise of buyer power by certain grocery retailers, through the adoption of supply chain practices that transfer excessive risks and unexpected costs to their supplies, was also a feature of the market for the supply of groceries which had an adverse effect on competition.[13] The remedies imposed by the Competition Commission included a requirement on grocery retailers to release restrictive land covenants and existing exclusivity arrangements in high concentration areas and not to enter into new restrictive arrangements of this kind, a recommendation to remove agreements relating to grocery retailing from the Competition Act Land Agreements Exclusion Order and the creation of a new Groceries Supply Code of Practice which regulates some of the terms and conditions between supermarkets and their suppliers.

17 In general, the OFT will only consider making a market investigation reference where it concludes that it is unlikely to be able to establish a breach of the Competition Act or Articles 101 and/or 102 TFEU, but remains concerned about the adverse effects on competition, or where the OFT considers that any action it might take under the Competition Act is likely to be ineffective.

1.2 Do these principles vary depending on the type of vertical practice considered?

18 In general, the legal framework does not vary depending on the type of vertical practice under consideration. The only circumstances in which the assessment of vertical agreements differs is in respect of "land agreements." This is because in the UK there is currently an exclusion from the Chapter I prohibition (although not Article 101 of the TFEU) in respect of "land

[11] Section 131(1) Enterprise Act.
[12] Section 138 Enterprise Act.
[13] *The Supply of Groceries in the UK,* Competition Commission Market Investigation report published on 30 April 2008 (**Competition Commission's Groceries Report**).

agreements" under the Competition Act 1998 (Land Agreements Exclusion and Revocation) Order 2004 No 1260 (**Land Agreements Exclusion Order**).

19 "Land Agreements" are defined in the Land Agreements Exclusion Order as agreements between undertakings that create, alter, transfer or terminate an interest in land.[14] The term "interest in land" includes "*any estate, interest, easement, servitude or right in or over land*" and includes licences. [15]

20 The original rationale for the Land Agreements Exclusion Order was to avoid the OFT having to deal with a large number of notifications of "land agreements" so that it could focus its resources on the most serious infringements of competition law. The vast majority of "land agreements" were not considered likely to appreciably restrict, distort or prevent competition in the UK or a significant part of the UK. If a "land agreement" was anti-competitive there was a mechanism in the Land Agreements Exclusion Order which enabled the OFT to withdraw the benefit of the exclusion in order to apply the Chapter I prohibition.

21 For some time the Land Agreements Exclusion Order has been regarded as something of an anomaly in the modern UK competition law regime. In its final report on the Supply of Groceries in the UK[16] the Competition Commission suggested that the UK Government consider repealing it altogether. Following a three month consultation period which ended on 4 November 2009, the Government announced on 13 January 2010 that it would revoke the Land Agreements Exclusion Order in April 2010. The revocation will take effect on 6 April 2011.

1.3 Is there a specific prohibition in the national competition act on all vertical practices pertaining to prices? If not, which ways of controlling the prices applied to end-users are permissible?

22 There is no specific prohibition in the Competition Act regarding vertical practices relating to prices. These practices are dealt with under the general prohibitions on anti-competitive agreements and conduct noted in response to question 1.1 above.

23 The UK position on vertical pricing practices essentially mirrors that in the EU in that resale price maintenance (**RPM**) is considered a "hardcore" restriction which removes the benefit of VABE and which will usually infringe the Chapter I prohibition. The OFT has indicated in its Guidance on Agreements and Concerted Practices (**OFT 401**) that "*[a]n agreement whose object is directly or indirectly to fix prices, or the resale prices of any product or service, almost invariably infringes Article 81 and/or the Chapter I prohibition.*"[17] The same is true in respect of conduct aimed at achieving RPM through indirect means. In this regard, the OFT has regard to the examples of indirect RPM found in the European Commission's Guidelines on Vertical Restraints[18] which include threats, intimidation, warnings, penalties, delay or suspension of deliveries or contract terminations in relation to observance of a given price level.

[14] Article 3 of the Land Agreements Exclusion Order.
[15] In Scotland, it also includes any interest under a lease and other heritable rights in or over land, including heritable securities.
[16] Competition Commission's Groceries Report, supra, footnote 13.
[17] OFT Competition Law Guide on *Agreements and concerted practices* (OFT 401, Edition 12/04) (**OFT 401**), paragraph 3.4.
[18] Supra, footnote 9.

24 Nevertheless, like the position under EU law under Article 101(3), an RPM agreement can in principle be exempted under section 9(1) of the Competition Act if it can be shown to be indispensable to achieving efficiency gains that benefit consumers and does not eliminate competition.

25 In common with the position under EU competition law, it is permissible for a supplier to impose a maximum sale price or to recommend a resale price under UK competition law, provided that they do not amount to a fixed or minimum sale price as a result of threats from, or incentives offered by, any of the parties. An example of the analysis of recommended retail prices under UK competition law can be seen in the 2003 decision regarding certain selective distribution arrangements between Lladró Comercial SA (**Lladró**) and a large number of UK retailers by the OFT).[19] In that case:

- Lladró imposed an obligation on retailers to inform Lladró in advance of any intention to sell below RRP and entitled Lladró to re-purchase such products. The agreements also expressly prohibited retailers from advertising discounts or price reductions on Lladró products.

- The OFT found that the obligation on retailers to inform Lladró of proposed discounts had the obvious consequence of restricting the buyer's ability to determine its own resale prices and amounted to pressure not to resell below and a disincentive not to sell below the recommended level. Equally, Lladró's entitlement to repurchase the products in question at cost price was considered to restrict the buyer's ability to determine its own resale prices. These provisions were therefore considered to have as their object the prevention, restriction or distortion of competition.

- As regards the advertising restriction, the OFT considered that any provision which restricts a retailer's freedom to inform potential customers of discounts which are being offered removes a key incentive for, and constitutes an obstacle to, price competition between retailers. This is because such a provision makes it more likely that retailers will not deviate from the recommended price thereby limiting the latter's ability to compete on price. The OFT therefore concluded that such a provision has as its obvious consequence the restriction of a retailer's ability to determine its own resale prices and therefore has as its object the prevention, restriction or distortion of competition.

1.4 What is the de minimis / appreciability threshold, if any, applicable to vertical arrangements and practices?

26 A vertical agreement or concerted practice will only fall within the Chapter I prohibition if it has as its object or effect an appreciable prevention, restriction or distortion of competition within the UK which may affect trade within the UK. [20] Indeed, as noted above in response to

[19] *Agreements between Lladró Comercial SA and UK retailers fixing the price of porcelain and stoneware figurines,* Decision of Director General of Fair Trading, No CA98/04/200331 March 2003. (OFT *Lladro*)

[20] The OFT has indicated that its focus will be on the effect on competition, as in practice it is very unlikely that an agreement which appreciably restricts competition within the UK does not also affect trade within the UK (OFT 419, paragraph 2.2).

question 1.2, one of the reasons why the Land Agreements Exclusion Order was put in place was that the UK Government considered that the vast majority of "land agreements" were not likely to appreciably restrict, distort or prevent competition in the UK or a significant part of it.

27 In determining whether an agreement has an appreciable effect on competition for the purposes of Article 101 and/or the Chapter I prohibition, the OFT has regard to the EU thresholds on appreciability contained in the European Commission's Notice on Agreements of Minor Importance.[21] As a matter of practice, the OFT is likely to consider that an agreement will not fall within either Article 101 or the Chapter I prohibition when it is covered by the Notice on Agreements of Minor Importance.[22]

28 Therefore, in the case of an agreement between non-competing undertakings,[23] the agreement will not appreciably restrict competition for the purposes of Article 101 and/or the Chapter I prohibition if the market share of each of the parties to the agreement does not exceed 15 per cent on any of the relevant markets affected by the agreement. That threshold will, of course, reduce to five per cent where competition on the relevant market is restricted by the cumulative foreclosure effect of parallel networks of agreements having similar effects on the market.

29 The threshold above does not apply to an agreement which contains one or more of the restrictions set out in paragraph 11 of the Notice on Agreements of Minor Importance. These include, in the case of an agreement between non-competing undertakings, a provision which:

- limits a buyer's ability to determine its resale price;
- restricts a buyer operating at a retail level from selling to any end user in response to an unsolicited order (passive selling); or
- restricts active or passive selling by the authorised distributors to end-users or other authorised distributors in a selective distribution network; or
- restricts, by agreement between a supplier of components and a buyer who incorporates those components in its products, the supplier's ability to sell the components as spare parts to end-users or independent repairers not entrusted by the buyer with the repair or servicing of its products.

30 Agreements containing any of these restrictions are regarded as being capable of having an appreciable effect even where the market shares are below the threshold set out above.

31 In any event, the OFT has indicated that the fact that the parties' market shares exceed the threshold set out above does not mean that the effect of an agreement on competition is appreciable. It will also consider other factors in determining whether the agreement has an

[21] OJ 2001 C368/13.
[22] Indeed, the OFT has indicated that where undertakings have in good faith relied on the terms of that Notice, the OFT will not impose financial penalties for an infringement of Article 101 and/or the Chapter I prohibition. (OFT Guidance on Agreements and Concerted Practices (OFT 401) December 2004 paragraph 2.19).
[23] i.e. undertakings which are neither actual nor potential competitors on any of the markets concerned.

appreciable effect. Relevant factors may include for example, the content of the agreement and the structure of the market(s) affected by the agreement, such as entry conditions or the characteristics of buyers and the structure of the buyers' side of the market.[24]

1.5 Has the competition authority in your jurisdiction issued guidelines regarding exchanges of information and/or vertical price agreements?

32 The OFT has not issued specific guidelines regarding exchanges of information and/or vertical price agreements. However, there is some general guidance on information sharing in the OFT's Competition Law Guide on *Agreements and Concerted Practices*[25] which also appears in similar terms in the OFT's Competition Law Guide on *Trade Associations.*[26] The general approach of the OFT to information exchange is based on the relevant principles established by the European Court.

33 The OFT recognises that, in the normal course of business, undertakings exchange information legitimately in relation to a number of matters which are of no risk to the competitive process and that, in certain circumstances, competition may be enhanced by information sharing. However, the OFT goes on to state that the exchange of information may have an adverse effect on competition where it serves to reduce or remove uncertainties inherent in the process of competition (consistent with the position under EU competition law).

2. Criteria applicable to price related vertical agreements

2.1 Is the national competition act declaring these or some of these practices as illegal under a per se rule, presumption or rule of reason?

34 The Competition Act does not contain any specific provisions in relation to price related vertical agreements. However, section 60 of the Competition Act requires the OFT and UK courts, in so far as possible, to deal with questions arising in relation to the Chapter I prohibition in a manner consistent with the treatment of corresponding questions arising under EU law.

35 In practice, the OFT considers that an agreement or concerted practice whose object is directly or indirectly to fix the resale price of any product or service, almost invariably infringes the Chapter I prohibition and that such arrangements, by their very nature, restrict competition to an appreciable extent.[27] This approach applies to both direct and indirect RPM. The OFT's approach is in line with that adopted by EU jurisprudence in that RPM is regarded as a prima facie infringement that has both the object and effect of restricting competition between retailers.

2.2 Are only agreements pertaining to prices considered illegal? Which conditions have to be fulfilled in order to render "agreements" to be considered illegal?

[24] OFT 401, paragraph 2.20.
[25] Ibid., paragraphs 3.17 to 3.21.
[26] OFT Competition Law Guide on *Trade Associations, professions etc* (OFT 408), paragraphs 3.4 to 3.13.
[27] OFT 401, paragraph 3.4.

36 It is not only "agreements" relating to prices that may be considered illegal. The Chapter I prohibition applies to "concerted practices" as well as "agreements",[28] including indirect concerted practices as described further below in response to question 2.3.

Agreements

37 The conditions which have to be fulfilled to establish the existence of an agreement within the meaning of the Chapter I prohibition mirror the position under EU law. There will be an agreement for the purposes of the Chapter I prohibition where there is a "concurrence of wills" (i.e. where a group of undertakings adhere to a common plan that limits, or is likely to limit, their commercial freedom by determining the lines of the mutual action, or abstention from action).[29]

38 It is not however, necessary to establish a joint intention to pursue an anti-competitive aim. Equally, the form in which the parties' intention to behave on the market is expressed is irrelevant, so that an agreement does not have to be in writing and there is no requirement that it be legally binding or contain any kind of enforcement mechanism. An agreement may also be express or implied from the conduct of the parties.

Tacit acquiescence

39 It is also possible for an agreement to be made tacitly between the parties. Tacit acquiescence requires an express or implied "invitation" from one party to the other party to fulfil an anti-competitive goal "jointly", which may be inferred from conduct. For example, where a manufacturer adopts certain measures in the context of its ongoing contractual relations with its retailers, such measures will amount to an agreement if there is express or implied acquiescence or participation by the retailers in those measures.

Concerted practice

40 The Chapter I Prohibition also applies in respect of concerted practices. A concerted practice does not require an actual agreement (whether express or implied) to have been reached. The OFT follows the ECJ case law in this regard in that the Chapter I Prohibition will capture a "*form of co-ordination between undertakings which, without having reached the stage where an agreement properly so called has been concluded, knowingly substitutes practical co-operation between them for the risks of competition.*"[30]

41 In particular, a concerted practice may occur where there are reciprocal contacts between undertakings which have the object or effect of removing or reducing uncertainty as to their future conduct on the market.[31] Therefore, in order to prove concertation, it is not necessary to show that a party has formally undertaken, in respect of one or several others, to adopt a particular course of conduct, or that the competitors have expressly agreed a particular course

[28] Section 2(1) Competition Act.
[29] *JJB Sports PLC and others v OFT* [2004] CAT 17 at 155 –157 and 637; *Argos Limited and Littlewoods Limited v OFT* [2004] CAT 24 at 150-153 and 658; and (1) *Argos Limited and (2) Littlewoods Limited and OFT and JJB Sports plc and OFT*, [2006] EWCA Civ 1318, paragraphs 21-27.
[30] Case 48/69 *ICI Ltd v European Commission* [1972] ECR 1969 at paragraph 64.
[31] Ibid., paragraph 175.

of conduct on the market. It is sufficient that, by its statement of intention, a party should have eliminated or, at the very least, substantially reduced uncertainty as to the conduct on the market to be expected on his part.[32]

42 The prohibition of concerted practices prohibits any direct or indirect contact between undertakings, where the object or effect is either to influence the conduct on the market of an actual or potential competitor or to disclose to such a competitor the course of conduct which they themselves have decided to adopt or contemplate adopting on the market.[33] This contact may take effect within the context of a horizontal relationship between competitors or within the context of a vertical relationship between undertakings operating at different levels of the market. Equally, such contact may take effect directly between competing undertakings or indirectly through an intermediary.[34]

2.3 What about the situations which are in-between, such as recommendations / suggestions and exchange of information?

Recommendations/suggestions

43 As noted above in response to question 1.3, the position under UK competition law in relation to recommendations and suggestions essentially mirrors that under EU competition law. However, one point of difference relates to the Restriction on Agreements and Conduct (Specified Domestic Electrical Goods) Order 1998/1271 (the **Domestic Electrical Goods Order**). This Order, which was made under the Fair Trading Act 1973, prohibits the use of recommended retail prices for certain domestic electrical goods and was intended to increase price competition in the domestic electrical goods market. Article 2 of the Domestic Electrical Goods Order prohibits suppliers of camcorders, cold food storage equipment, dishwashers, hi-fi-systems, televisions, tumble dryers, video cassette recorders or washing machines) from recommending or notifying a price at which those goods should be sold.

Information exchange

44 One area of particular interest in UK competition law currently is the approach that the OFT and UK courts have been taking in respect of exchanges of commercially sensitive information between competitors via a mutual intermediary (so-called "hub and spoke" arrangements). This approach can be seen in two cases from 2003 relating to sales of, respectively, replica football kit (*Replica Kit*), and toys and games (*Toys*). Both OFT decisions (OFT *Replica Kit*[35] and OFT *Toys*[36]) were appealed to the Competition Appeal Tribunal (**CAT**), whose decisions

[32] *JJB Sports plc v OFT* and *Allsports Ltd v OFT* [2004] CAT 17, at 872.
[33] Cases 40/73 etc *Suiker Unie v Commission* [1975] ECR 1663 at paragraph 174.
[34] Ibid, paragraph 643.
[35] Case CA98/06 [2003] OFT (OFT *Replica Kit)*
[36] Case CA98/02 [2003] (OFT *Toys)*

(CAT *Replica Kit*[37] and CAT *Toys*[38]) were subsequently appealed to the Court of Appeal and largely upheld (in a combined judgment (CA *Replica Kit and Toys*[39]).

Replica Kit – OFT and CAT

45 In OFT *Replica Kit*, the OFT found that Umbro had entered into vertical agreements with a number of downstream retailers to fix the retail price of certain replica football kits. The OFT found a number of agreements or concerted practices, one of which concerned the relationship between: (i) JJB Sports PLC (**JJB**), the largest sports retailer in the UK; (ii) Umbro, the manufacturer of England and Manchester United replica kit at the relevant time; and (iii) Sports Soccer, another retailer of replica kit. In particular, the OFT found that:

- JJB had put pressure on Umbro (as supplier) to take action in response to aggressive discounting by its retail competitor, Sports Soccer.
- During conversations with Umbro, JJB gave an assurance or, at least, an indication that it would not price below the recommended retail price (RRP) of £39.99 during the Euro 2000 tournament, in circumstances in which it was obvious that this information would or might be passed on to Sports Soccer, so as to help Umbro persuade Sports Soccer not to discount below RRP.
- Umbro did in fact pass this information on to Sports Soccer.
- Sports Soccer agreed to (and did in fact) raise its prices in reliance on this information.
- Umbro also told JJB of this, thereby making it clear to JJB that it would be able to maintain its prices at RRP, which JJB did.

46 The CAT and the Court of Appeal agreed with the OFT that this sequence of events amounted to a concerted practice to which JJB was a party, as well as Umbro and Sports Soccer, whereby the two retailers coordinated their conduct on the market in such a way as to knowingly substitute practical cooperation between them for the risks of competition. The concerted practice had the object of restricting competition and in particular of fixing the retail sale price of England replica football shirts, and therefore constituted a breach of the Chapter I prohibition.

47 When the OFT's decision was appealed to the CAT, the CAT relied on the fact that, in the context of concerted practices, European case law prohibits both direct and indirect contact between undertakings so that it did not make any difference that in *Replica Kit* the reciprocal

[37] *JJB Sports plc v OFT and AllSports Ltd v OFT* [2004] CAT 17 (CAT *Replica Kit*)
[38] *Argos Limited and Littlewoods Limited v OFT* [2004] CAT 24 (CAT *Toys*)
[39] Combined judgment: *Argos Limited and (2) Littlewoods Limited and OFT and JJB Sports plc and OFT*, [2006] EWCA Civ 1318 (CA *Replica Kit and Toys*)

contact had taken place through the intermediary of Umbro.[40] The CAT considered that an indirect concerted practice would exist in circumstances where:

- Retailer A disclosed its future (retail) pricing intentions to Supplier B;
- it was reasonably foreseeable that Supplier B might make use of that information to influence market conditions; and
- Supplier B passed that pricing information on to a competing retailer C.

Toys – OFT and CAT

48 In OFT *Toys*, the OFT found that Hasbro, a leading global manufacturer of toys and games and one of the largest toys and games suppliers in the UK, had entered into vertical agreements with Argos and Littlewoods, two major high street catalogue-based retailers in the UK, to fix the price of certain Hasbro toys and games at Hasbro's recommended retail price (**RRP**). The infringement consisted of two vertical bilateral agreements – one between Hasbro and Argos and the other between Hasbro and Littlewoods – to fix prices for certain Hasbro products at Hasbro's RRPs and a trilateral agreement, with a horizontal component, between Hasbro, Argos and Littlewoods to the same effect.[41]

49 Upon appeal, the CAT applied the same formula in its assessment of evidence of indirect exchanges of future pricing intentions by competing toy retailers in *Toys.*[42] It upheld the OFT's finding that, in addition to there being two bilateral agreements between Hasbro and each of the retailers to sell the relevant Hasbro products at Hasbro's RRPs, there was also a trilateral concerted practice between Hasbro, Argos and Littlewoods.

Court of Appeal

50 The Court of Appeal considered the *Replica Kit* and *Toys* appeals at the same time and concurred with the CAT's view that indirect concerted practices existed in both cases. However, the Court of Appeal suggested that, when establishing whether a concerted practice existed, the CAT' "*may have gone too far*" if it intended that its test would extend to cases in which Retailer A did not, in fact, foresee that that Supplier B would make use of its pricing information to influence market conditions or in which Retailer C did not, in fact, appreciate that Retailer A's pricing information was being passed to it with Retailer A's concurrence.[43] In

[40] CAT *Replica Kit*, paragraph 657

[41] The infringement arose because Hasbro had sought to persuade retailers to retail Hasbro products at Hasbro's RRPs, The participation of both Argos and Littlewoods was essential to the success of the initiative. However, Argos, which was generally regarded as the price-setter, would have been unlikely to agree to the scheme unless it had reassurance that in doing so, its catalogue prices would not be undercut by Littlewoods. Therefore, if the scheme were to succeed, it was necessary for Hasbro to be in a position to reassure Argos that Littlewoods would also be committed to follow the same prices. As a result, two separate sets of discussions took place between Hasbro's sales team and the relevant buyers for Argos, on the one hand, and between Hasbro's sales team and the relevant buyers for Littlewoods, on the other. There was no evidence of direct contact between Argos and Littlewoods. Nevertheless, following those discussions, there was a price similarity in those retailers' catalogues in relation to the products subject to the pricing initiative.

[42] CAT *Toys*, paragraph 779.

[43] CAT *Replica Kit*, paragraph 91

doing so, it distinguished bilateral discussions between a supplier and distributor on actual or likely retail prices and profit margins from discussions that stray into intended prices and agreements on future prices. The CAT in the earlier appeal had recorded that price information exchanged in the form of a retailer revealing its future pricing intentions to its supplier will rarely be "legitimate" otherwise RPM could be reintroduced by the back door.[44] However, the Court of Appeal recognised the necessity of bilateral pricing discussions between supplier and retailer. It considered that such discussions are unobjectionable so long as the pricing information is not provided in order to be shared.[45]

51 The Court of Appeal went on to set out a slightly modified formulation of the CAT's framework, which it regarded as consistent with European law and sufficient to dispose of the appeals in the *Toys* appeal.[46] That modified framework states that if:

- Retailer A discloses to supplier B its future pricing intentions in circumstances where A may be taken to intend that B will make use of that information to influence market conditions by passing that information to other retailers (of whom C is or may be one);

- B does, in fact, pass that information to C in circumstances where C may be taken to know the circumstances in which the information was disclosed by A to B; and

- C does, in fact, use the information in determining its own future pricing intentions

then A, B and C are all to be regarded as parties to a concerted practice having as its object the restriction or distortion of competition.

52 The Court of Appeal went on to state that the case will be stronger where there is reciprocity in the sense that C discloses to supplier B its future pricing intentions in circumstances where C may be taken to intend that B will make use of that information to influence market conditions by passing that information to (amongst others) A, and B does so.

2.4 What is the assessment of vertical unilateral practices in relation to prices?

53 Provided that the vertical practice is genuinely unilateral and it is not possible to show there was "tacit acquiescence" so as to give rise to an agreement or concerted practice, then Article 101 and the Chapter I Prohibition will not apply. However, vertical unilateral practices relating to prices entered into by an undertaking which holds a dominant position in a market may be subject to Article 102 and/or the Chapter II prohibition.

54 It should be noted that it is possible to establish a concerted practice where pricing or other market sensitive information is disclosed unilaterally by one party to another in circumstances

[44] CAT *Replica Kit* , paragraph 660
[45] CA *Toys and Replica Kit*, paragraphs 99 and 106
[46] CAT *Toys,* paragraph 141

where that information is at the very least accepted by the recipient or the recipient does not express any reservations or objections.[47]

55 Similarly, the mere receipt of information concerning competitors' future pricing intentions may be sufficient to give rise to concertation.[48] In *Aalborg Portland*, the ECJ stated than an undertaking which receives information by participating in meetings without manifestly opposing the anti-competitive agreements concluded will be taken to have participated in a concerted practice unless that undertaking puts forward evidence to establish that it had indicated its opposition to the anti-competitive arrangements to its competitors.[49]

56 Where an undertaking participating in concerted arrangements remains active on the market, there is a presumption that it will take account of the information exchanged with its competitors. The EC courts and the CAT have re-stated this principle in a number of judgments. In its judgment in *Replica Kit*, the CAT, relying on EU jurisprudence stated that "*[e]ven where participation in a meeting is limited to the mere receipt of information about the future conduct of a competitor, the law presumes that the recipient of the information cannot fail to take that information into account when determining its own future policy on the market*."[50]

2.5 Are some of these practices not considered illegal merely as a result of a de minimis/appreciability rule?

57 As noted in response to question 1.4 above, the OFT is likely to consider that an agreement will not fall within either Article 101 or the Chapter I prohibition when it is covered by the European Commission's Notice on Agreements of Minor Importance.[51] Therefore, where the agreement is made between non-competing undertakings, the OFT will not consider competition to be appreciably restricted if the market share of each of the parties on any of the relevant markets affected by the agreement or concerted practice does not exceed 15 per cent.

58 However, this approach does not apply to agreements or concerted practices that limit a buyer's ability to determine its resale price.[52] Such agreements or concerted practices are regarded as being capable of having an appreciable effect even where the market shares fall below the relevant thresholds, provided that such agreements do not have only insignificant effects.[53]

3. Anti-competitive effects

[47] Cases T-202/98, T-204/98 and T-207/98 *Tate & Lyle plc v Commission* [2001] ECR II 2035 and Cases T-25/95 etc *Cimenteries CBR SA v Commission* [2000] ECR II-491 at paragraph 1849, referred to in CAT Toys, paragraph 154.
[48] Cases T-202/98, T-204/98 and T-207/98 *Tate & Lyle plc v Commission* [2001] ECR II 2035 at paragraph 54.
[49] Cases C-204/00P, 205/00P,211/00P, 213/00P,217/00P and 219/*00P Aalborg Portland A/S v European Commission* [2004] ECR I-123, at paragraph 81 ff.
[50] CAT *Replica Kit*, at 873.
[51] Indeed, the OFT has indicated that where undertakings have in good faith relied on the terms of that Notice, the OFT will not impose financial penalties for an infringement of Article 101 and/or the Chapter I prohibition. (OFT 401, paragraph 2.19).
[52] OFT 401, paragraph 2.17.
[53] OFT 401, paragraph 2.16 and 2.17.

3.1 Are the anti-competitive effects considered by the national competition act different for each of these practices, or is it always the same kind of anti-competitive effect which is considered and found more or less serious?

59 National competition law which, as noted, largely mirrors Articles 101 and 102 TFEU, does not delineate the possible effects of different types of vertical practice. However OFT 419 (the OFT's Guidance on Vertical Agreements), which largely follows the economic logic of Regulation 2790/99/EC and the associated European Commission Guidelines on Vertical Restraints,[54] identifies market foreclosure and competition dampening as possible anti-competitive effects of vertical restraints.

Market foreclosure

60 Selective distribution may lead to market foreclosure at retail level if it is practised by a sufficient proportion of manufacturers, particularly where retailers are limited numerically and not just through the imposition of (objective) qualitative criteria. If a sufficient number of popular brands are distributed through similar selective distribution agreements (resulting in relatively few retailers stocking the full range of popular brands), there may be insufficient competition from "independent" retailers to act as an effective constraint on manufacturers. Manufacturers may thus be put in a position to exercise a degree of market power (which may result in possible foreclosure effects).

Competition dampening

61 Competition dampening can occur in various ways. RPM is regarded as having direct negative effects on intra-brand competition. OFT 419 also notes that RPM may be a means for collusion, for example by making it easier to detect variation from (collusively) agreed prices.

62 This area of competition law - of RPM combined with collusion - has been the focus of recent OFT investigation and infringement decisions under the Chapter 1 prohibition and is where the major developments in relation to RPM are occurring in the UK. *Toys* and *Replica Kits,* already discussed at 2.3, both involved RPM that broadened into horizontal collusion. Each case involved vertical RPM agreements and a "horizontal" collusive agreement (based on information exchange). The vertical restraints took the form, in each case, of agreements or understandings between, respectively, the supplier and each of (at least) two retailers, under which the retailers would adhere to, or closely to, identified resale prices. In *Toys* this was the recommended resale price and in *Replica Kit* the "High Street price", which was set by the retailer with greatest market power, at a small discount from the recommended resale price. The further collusive arrangement with a "horizontal" component was, in each case, between the supplier and the relevant retailers. These horizontal arrangements came about because the pricing intentions of the retailers (to adhere to resale prices) were made known to each other through the medium of the supplier, but without evidence of any direct contact between the retailers. This is referred to as a "hub-and-spoke" arrangement.

63 OFT 419 notes that competition dampening effects can result from other types of vertical arrangement, such as exclusive dealing. Where manufacturers distribute to exclusive retailers,

[54] Supra, footnote 9

in store inter-brand competition is eliminated because each retailer only sells one brand. (Intra-brand competition may also be reduced.) Where retailers are in different locations it becomes more difficult for customers to compare and select a different manufacturer's product, making each manufacturer's product less price sensitive and dampening inter-brand competition at manufacturing level.

64 OFT 419 also recognises the mutually reinforcing effect of combinations of vertical restraints. So, for example, selective distribution combined with full-line forcing may lead to retailers stocking only one manufacturer's products rather than a number of competing products. Similarly, minimum purchase requirements may, in practice, result in exclusive dealing.

3.2 To which extent is the national competition act considering only inter-brand effects or does it consider intra-brand effects?

65 As noted above in response to question 3.1, OFT 419 discusses the potential effects of different vertical practices in terms of both intra-brand and inter-brand competition. In addition to reducing intra-brand competition, RPM is regarded as having the potential to facilitate collusion and affect inter-brand competition. Exclusive distribution reduces intra-brand competition and inter-brand competition at the retail level, as a result of exclusivity. Where retailers operate in distinct geographic locations, inter-brand competition may be affected at the manufacturing level, as demand from retailers becomes less price sensitive.

3.3 Is also the anti-competitive intent of the vertical agreement considered?

66 Under UK competition law, agreements which are anti-competitive by object and agreements which are anti-competitive by effect infringe the Chapter 1 prohibition. Where an agreement is found to be anti-competitive by object, there is no need to consider the effects of the practice.[55] Agreements which have the object of restricting a buyer's freedom to determine resale prices are presumed to have anti-competitive effects.[56]

67 In considering whether an agreement is anti-competitive by object (has as its object the prevention, restriction or distortion of competition), the OFT will consider the aims of the agreement in the economic context in which it operates. The assessment of the aims of the agreement will be determined by an objective assessment of the meaning and purpose of the agreement, rather than by any consideration of the subjective intention of the parties when entering into the agreement. In this respect the OFT takes the view that if the obvious consequence of an agreement is to prevent, restrict or distort competition, that will be its object notwithstanding that it may have other aims as well.[57]

68 In accordance with EU competition law, restrictions that are anti-competitive by object are broadly equivalent to those listed as hardcore restrictions, which are regarded as unlikely to

[55] for example, OFT *Replica Kit*, paragraph 495, following Case 56/65 *Société Technique Minière v Maschinenbau Ulm* ; Cases 56 and 58/64 *Consten and Grundig v European Commission* ; Case C-199/92 *P Hüls v European Commission*;Joined Cases T-374/94 et seq *European Night Services v European Commission*

[56] OFT *Lladro* noted (paragraph 59): "*A provision in an agreement which, directly or indirectly, in isolation or in combination with other factors under the control of the parties, has the object of restricting the buyer's ability to determine the prices at which goods or services are resold by the buyer will prevent, restrict or distort competition".*

[57] OFT *Lladro* paragraph 57, following Cases 96-102, 104, 105, 108, 110/92 *IAZ v Commission*

qualify for exemption.[58] The anti-competitive object of an agreement would be taken into account for the purpose of calculating any fine to be imposed. The subjective intention of the parties to the infringement would also be taken into account at this stage (see the response to question 5.3 below).

3.4 Do the courts take into account the actual acts performed by the supplier, e.g. if the supplier, in practise encourages a recommended price to constitute a fixed price through punishments or remunerations? Please give examples from case law and/or legal doctrine.

69 The conduct of the supplier may well be taken into account to support a finding of infringement. Conduct that has the effect, in practice, of fixing recommended prices as minimum or fixed resale prices would be taken into account. In these circumstances, the practice is likely to be treated as fixed RPM and more liable to be presumed to be anti-competitive.

70 In its decision in *Lladro* the OFT noted:[59]

> *"A provision in an agreement allowing a supplier to provide a recommended resale price will not in itself infringe the Act. However, this will not be the case where the recommended resale price amounts to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties. The Director takes the view that any such pressure or incentive distorts free competition in that resellers become constrained by factors other than those which condition the normal competitive process."*

71 In *Toys* and *Replica Kit*, conduct by the manufacturers to persuade retailers to adhere to RRPs took the form of the manufacturer communicating each retailer's pricing intentions to the other in order to give comfort that each would adhere to RRPs and not undercut the other. As noted above, this conduct broadened the bilateral vertical arrangements to create a further collusive arrangement with a horizontal component. There was also evidence in *Replica Kits* that the manufacturer made (veiled) threats to one of the retailers,[60] but in the context of the case this was not relied on to support the findings of infringement.

4. Pro-competitive effects

4.1 Does the national competition act recognise justifications in relation to these vertical practices regarding prices? Has the relevant case law taken into account practical justifications for the need of price agreements and/or pro competitive aspects in relation to the exchange of information regarding price?

72 In the UK, it is recognised that vertical agreements that infringe the Chapter 1 prohibition may be justified because they produce recognised benefits, even where they are not block exempted (by parallel exemption under VABE). As a result, vertical agreements generally

[58] Guidelines on Vertical Restraints, see (supra footnote 9)
[59] OFT *Lladro* paragraph 60
[60] for example, see CAT *Replica Kit* paragraph 43

need to be assessed on a case by case basis and, where found to infringe the prohibition, considered against the exemption criteria in section 9(1) of the Competition Act. While price fixing agreements are regarded as hardcore infringements, it may in rare cases be possible to justify RPM where it is necessary to achieve efficiency gains that benefit consumers, provided competition is not eliminated. However, subject to certain historical exceptions (which are discussed below), there have been no cases where RPM has qualified for an exemption.

Net Book Agreement

73 Under the *Net Book Agreement* (**NBA**), which was in place from 1900 to 1997, retailers were prevented from selling books at less than the publisher's RRP. The NBA was exempted under previous competition legislation on justifications that stemmed from an acceptance that "books are different".[61] The justifications were: (i) that the production and distribution of books necessitated different treatment from other goods (to mitigate the risks associated with the lengthy pre-sale process, through predictable retail volumes); and (ii) that books were so important to national culture and had such a particular social and educational role to play that they should be protected from the rigours of competition law. The NBA was exempted because it was thought to be necessary for maintaining existing levels of booksellers in order to keep prices down overall and, in turn, protect the publication of marginal books.[62]

74 The NBA started to break down in the mid-1990s partly due to changes in the industry, reinforced by the European Commission's 1988 decision that it infringed Article 85(1) because of cross-border effects (UK/Ireland). The Book Publishers abandoned the NBA in 1995 and it was formally dismantled by the Restrictive Practices Court in 1997.[63] The Court discounted the earlier justifications for the exemption. It disagreed that abolition of the NBA would cause uncertainty in demand and reduce retailer orders thus reducing manufacturing efficiencies and resulting in cost increases. New production methods for book production and shorter delivery times, together with "sale or return" policies, would lessen any impact on ordering. The Court also considered that the effect of the NBA's abolition on the production of titles would be minor. While returns from book writing might decrease, this would not necessarily mean fewer titles would be written and published.

75 A report by the OFT on the impact of the end of the NBA on overall productivity in book retailing and publishing suggests that, contrary to some expectations, total book sales volumes have increased, the number of titles published has increased and there has been an increase in retail diversity (new "bricks and mortar" entry and on-line sales to consumers (Amazon)).[64] The study suggests these developments would have been slower had RPM remained in place, leading to the conclusion that the NBA had negative inter-firm effects. One surprising finding, however, was that intra-firm efficiency did not improve over the same period. The study suggests that this was partly because a lot of efficiency improvement had already occurred prior to the removal of RPM, when the NBA was already breaking down.

[61] Net Book Agreement 1957 (No. 1) [1962] 1 WLR 1347

[62] The argument ran that, without the net book agreement, many stockholding booksellers would be driven out of business; that those stockholding booksellers who survived would inevitably have to increase overall prices substantially and so publishers would not publish marginal books which have most literary and scholastic merit;

[63] Net Book Agreement 1957 (No. 4) [1998] ICR 753

[64] An evaluation of the impact upon productivity of ending RPM on books (June 2008) at http://www.oft.gov.uk/shared_oft/economic_research/oft981.pdf

Nonetheless, the overall conclusion of the report is that the NBA caused competitive harm by preventing downstream entry and was not needed for maintaining sales volume or diversity.

Medicines

76 In *Medicines,*[65] another case in which an exemption granted for RPM under previous legislation was removed following the advent of the Competition Act, the Restrictive Practices Court found in 1970 that RPM was necessary to ensure that chemist shops were not increasingly put out of business by supermarkets to the consequent detriment to the public. It was also concerned that full-line wholesalers, who stocked the less popular and less profitable products, would be forced to reduce their delivery service to retail chemists.

77 In 1999. the OFT applied to have the exemption in the *Medicines* case removed on grounds of a material change in the retailing of pharmaceuticals and of the circumstances found by the Court in 1970. [66] The OFT considered that the abolition of RPM was necessary to bring lower prices to the public on a significant range of branded medicaments through increased competition between retail outlets and the resulting pressure on manufacturers to lower production and distribution costs. The RPM arrangement in *Medicines* was the last remaining the legally sanctioned RPM in the UK when it was finally overturned in 2001.

Other justifications advanced in relation to vertical pricing practices

78 In *Replica Kit* the Court of Appeal distinguished bilateral discussions between a supplier and distributor on actual or likely retail prices and profit margins from discussions that stray into intended prices and agreements on future prices. The CAT in the earlier appeal had recorded that price information exchanged in the form of a retailer revealing its future pricing intentions to its supplier will rarely be "legitimate" otherwise RPM could be reintroduced by the back door.[67] However, as noted at 2.3 above, the Court of Appeal considered that the CAT may have gone too far and recognised the necessity of bilateral pricing discussions between supplier and retailer. It considered that such discussions are unobjectionable so long as the pricing information is not provided in order to be shared.[68]

79 In *Toys* the supplier's sales director stated in evidence to the CAT[69] that the RPM had consumer benefits in the form of lower prices for games, as a result of lower costs. This point was not further elaborated or taken into account in the CAT's or Court of Appeal's findings.

80 In *Lladro* the OFT rejected justification arguments based on the need to protect IP rights (trademark and reputation/image).[70]

---

[65] In re Medicaments Reference (No. 2) [1970] 1 W.L.R. 1339

[66] In re Medicaments and Related Classes of Goods (No 3) [2001] I.C.R. 306

[67] CAT *Replica Kit* , paragraph 660

[68] CA *Toys and Replica Kit*, paragraphs 99 and 106

[69] CAT *Toys,* paragraph 656

[70] OFT *Lladro* noted, paragraphs 72 – 77: "*Discounts offered by retailers on trademark bearing goods, or advertisements relating to such discounts, do not impair or interfere with the essential function of a trademark, given that the identity of the origin of the goods bearing a trademark is not affected by the price at which those goods are sold….. The Director takes the view that restrictions amounting to RPM (whether directly or indirectly imposed), including those which restrict a retailer's ability to advertise resale prices, cannot be objectively justified on the grounds that they are necessary to protect the reputation or image of a trademark. In the Director's view, any such reputation*

4.2 What are the types of pro-competitive effects recognised in relation to vertical practices on prices?

81 OFT 419 notes that, while vertical restraints may lead to anti-competitive effects if combined with market power, they may also produce economic benefits by promoting efficiencies, non-price competition and investment and innovation.[71]

82 Manufacturers may be able to use vertical restraints to overcome "free-rider" problems through, for example, conditions in selective distribution arrangements requiring all retailers selling their products to provide demonstration services. Vertical restraints may also be justified for promoting investment and innovation. For example, if a retailer contributed to the cost of a manufacturer developing a new product, the retailer might, to protect its investment, require agreement from the manufacturer that, once developed, the product will be sold exclusively to the retailer for a reasonable period.

83 The European Commission's draft vertical guidelines[72] indicate that the Commission may be more willing in future to undertake a more economic assessment of RPM arrangements. The draft guidelines note a number of pro-competitive effects of RPM, such as providing distributors with the means of increasing their promotional efforts for a new brand or in a new market, or allowing the manufacturer to organise a co-ordinated short-term low price campaign within an exclusive or selective distribution system.[73] Where parties substantiate likely efficiencies from the inclusion of RPM in their arrangements and demonstrate that the exemption criteria in Article 101(3) are satisfied, the draft guidelines place the onus on the European Commission to assess, and not just to presume, the likely negative effects of RPM, before deciding whether the exemption criteria are met.[74] Although the UK authorities would not necessarily follow the approach of the new guidelines, the OFT is likely to regard the pro-competitive effects identified as persuasive (assuming this is retained in the final version of the guidelines).

4.3 Are the following types of justifications taken into consideration and if yes, in relation to which sort of practices and to which extent?

- **competitive oversight inside the distribution network**
- **price-level positioning of the products by a supplier**
- **consumers benefits in relation to a resale price cap**
- **consumers' interest in general (please specify)**
- **launching of a new product**
- **market positioning of a product**
- **promotional organisation**
- **after sale services**
- **coordination with consumers' information**
- **short term promotional campaigns.**

Please give examples from case-law and/or legal doctrine.

---

or image derives not from the supplier's ability to control the resale price of the products or services bearing the trademark, but from other factors, including (in particular) the actual quality of those products or services and the environment in which they are sold."

[71] OFT 419, paragraph 7.19

[72] Draft European Commission Notice: Guidelines on Vertical Restraints, published 28 July 2009 (IP / 09 / 1197)

[73] Ibid, paragraph 221

[74] Ibid, paragraph 220

84 Please see the responses to questions 4.1 and 4.2 above.

4.4 Does the national competition act and case law take into consideration other justifications?

85 National competition law does not specify the justifications that may be taken into account when assessing vertical pricing practices. It is therefore open to undertakings to raise other justifications on a case by case basis, where these are relevant to satisfying the exemption criteria.

4.5 Are pro-competitive effects automatically taken into consideration by the authorities / the courts or ought they be invoked by the interested parties?

86 Pro-competitive effects and justifications are not automatically taken into consideration. It is for the parties to an infringing arrangement who are claiming the benefit of exemption to justify their arrangement on the basis that the exemption criteria in section 9(1) Competition Act or Article 101(3) are satisfied.

87 Section 9(1) contains equivalent criteria to those contained in Article 101(3) and, as with that provision, the burden of proof is on the undertaking seeking to justify an agreement. Section 9(2) of the Competition Act provides that *"[i]n any proceedings in which it is alleged that the Chapter I prohibition is being or has been infringed by an agreement, any undertaking or association of undertakings claiming the benefit of [section 9(1) of the Competition Act] shall bear the burden of proving that the conditions of that subsection are satisfied.*"[75]

88 In the UK, the normal civil standard of proof on the balance of probabilities applies where an undertaking seeks to establish that an agreement is exempt.

4.6 Might any of these justifications have anti-competitive effects and are they considered in the national competition act and case law ?

89 It is possible that some justifications may have anti-competitive effects. This is not expressly addressed in the legislation, but these effects would need to considered when assessing the justifications for the arrangement against the exemption criteria.

4.7 Have these justifications led to the conclusions that the agreement is not covered by a prohibition on anti-competitive agreements or to an exemption from the competition rules?

90 As already noted, under current law, RPM is considered to be a hardcore restriction that is most likely to infringe the Chapter I prohibition and is rarely capable of exemption. The RPM arrangements in *Net Book Agreement* and *Medicines* (discussed above) were sanctioned under previous competition laws and in light of the particular nature and circumstances, at that time, of the markets in which they operated.

[75] See also *Independent Media Support Ltd v OFT* [2008] CAT 13, paragraph 17.

91 Following the US Supreme Court's decision in *Leegin,*[76] which marked a shift towards a "rule of reason" approach to RPM, the European Commission also appears to have opened the door to a reappraisal of RPM (see the response to question 4.2 above). It is possible that the UK authorities may, in turn, become more receptive to a reassessment, but it remains to be seen to what extent the OFT would be prepared to analyse (and accept) the pro-competitive effects of RPM, rather than simply treating it as an object infringement, or to accept justifications in terms of the exemption criteria.

4.8 In your opinion do the antitrust authorities sufficiently take into consideration the pro-competitive effects of some of these practices?

92 To the extent that RPM is to be regarded as a "hardcore" infringement for UK competition law purposes, it is arguable that potential pro-competitive effects are not sufficiently taken into account. There has been a reappraisal of the economic theory in this area, which recognises the need to take account of the benefits which may result from RPM in certain cases. There may be instances, for example where RPM is unobjectionable or even necessary. Treating all RPM in the same manner may lead to errors in the form of prohibiting activity that may be pro-competitive or allowing activity that is anti-competitive, both of which may lead to long-term harm.

93 This reappraisal of economic theory was recognised by the US Supreme Court in *Leegin Creative Leather Products, Inc. v. PSKS, Inc*. In that case, the Supreme Court concluded that continued treatment of such agreements as per se illegal under federal law was no longer appropriate. Instead, RPM will be subject to a "rule of reason" approach and will only be considered illegal if shown to have an overall adverse effect on competition in a particular area. In reaching that judgment, the Court noted that economics literature “was replete” with “procompetitive justifications for a manufacturer’s use of resale price maintenance,”

5. Sanctions

5.1 Is the national competition legislation sanctioning vertical practices in general and if yes through which forms of sanctions; administrative and/or criminal or other?

94 The OFT has a number of remedies at its disposal to enforce compliance with the Chapter I and Chapter II prohibitions and Articles 101(1) and 102. If the OFT has made a decision that an agreement or conduct infringes the Chapter I or II prohibition or the prohibition in Article 101 or 102, it may:

- give directions designed to bring the infringement to an end
- impose financial penalties of up to a maximum of 10 per cent of the undertaking's worldwide turnover in the last business year preceding the OFT decision
- apply to the courts for competition disqualification orders against directors of an undertaking involved in an infringement. Under such orders company directors may be disqualified from holding office as a company director, receiver or insolvency practitioner for a maximum of 15 years.

[76] *Leegin Creative Products Inc v PSKS Inc*, Supreme Court of the United States, 28 June 2007

95 Where the OFT has begun an investigation but not reached a decision, it may:

- accept commitments to take such action (or refrain from taking such action) as it considers appropriate
- in certain circumstances, give interim measures directions for the purposes of addressing the competition concerns it has identified.

96 The OFT also has powers to take criminal prosecutions against individuals alleged to have committed the "cartel offence" contrary to s 188 Enterprise Act 2002. This only applies to horizontal forms of collusion and does not extend to RPM.

97 As noted above at paragraph 93, the Enterprise Act 2002 empowers the OFT to seek a court order disqualifying a director of a company that has been found to have infringed competition law from acting as a director of any company for up to 15 years.[77] The Court must make a competition disqualification order where two conditions are satisfied:

- the relevant person is a director of a company which has breached competition law; and
- the court considers that that person's conduct makes him or her unfit to be concerned in the management of a company. [78]

98 In deciding whether a person is unfit to be concerned in the management of a company, the court must have regard to whether:

- his conduct contributed to the breach of competition law;
- his conduct did not contribute to the breach but he had reasonable grounds to suspect that the conduct of the undertaking constituted the breach and he took no steps to prevent it;
- he did not know but ought to have known that the conduct of the undertaking constituted the breach.

The court may also have regard to his or her conduct as a director of a company in connection with any other breach of competition law.

5.2 Are the above practices subject to sanctions as well?

99 Vertical pricing restraints are subject to the sanctions noted above (with the exception of criminal sanctions for the cartel offence). The OFT may only impose a penalty where it is satisfied that the infringement has been committed intentionally or negligently by the undertaking. This is subject to limited immunity for so-called small agreements and conduct of minor significance.

---

77 S 204 of the EA 2002 introduced new provisions into the Company Director Disqualification Act 1986 (**CDDA**) which sets out the circumstances in which a court may, or must disqualify an individual from acting as a director of a company.

78 S 9A of the CDDA.

100 A party to a so-called 'small agreement' is immune from the imposition of penalties in respect of that agreement. Small agreements are agreements between undertakings with a combined turnover of in the calendar year preceding the infringement not exceeding £20 million.[79] However price–fixing agreements are excluded from this category. The OFT may also withdraw the small agreements immunity in individual cases.

5.3 Is the specificity of vertical relationships, for instance the lesser harm in relation to intra-brand restrictions, taken into consideration in the application of sanctions?

101 The OFT calculates the level of fines to be imposed on an infringing undertaking according to a step-by-step process set out in its fining guidelines.[80] The starting point for the fine is calculated having regard to the seriousness of the infringement and the relevant turnover of the undertaking. In determining the seriousness of the infringement, the OFT considers a number of factors including the nature of the infringement, the nature of the product and the damage caused to consumers.

102 In *Replica Kit*, the OFT acknowledged that it regarded horizontal price-fixing as the most serious type of competition infringement, and more serious (in that case) than RPM. Nevertheless, it is clear that RPM, as a hard core infringement, will attract significant penalties.

5.4 What are the major fines in your jurisdictions (in EUR) for vertical restraints? In which context have they been imposed? What is the major criminal or other sanction imposed?

103 The highest fines for vertical restraints were imposed in Toys and Replica Kit Following all appeals, these totalled £22.65m (€25.14m) in Toys and £15.5m (€17.20m) in Replica Kit. These figures were broken down as follows:

104 *Toys* (19 February 2003)

- Hasbro: Nil (reduced from £15.59m due to the OFT's leniency policy)
- Argos: £15m (reduced from £17.28m on appeal to the CAT)
- Littlewoods: £4.5m (reduced from £5.37m on appeal to the CAT).

105 *Replica Kits* (16 May 2002)

- JJB: £6.7m (reduced from £8.373m on appeal to the CAT, which determined that the OFT did not properly prove part of its case)
- Umbro: £5.3m (reduced from £6.641m on appeal to the CAT, which determined that the OFT did not properly prove part of its case)
- Manchester United Football Club: £1.5m (reduced from £1.652m on appeal to the CAT in recognition of MUFC's admission of wrongdoing and subsequent compliance programme)

[79] Competition Act 1998 (Small Agreements and Conduct of Minor Significance) Regulations 2000, SI 2000/262, regulation 3
[80] OFT Guidance as to the appropriate amount of a penalty, December 2004 (OFT 423)

- Allsports: £1.35m (increased from £1.42m by the CAT, which revoked the 5% reduction by the OFT for compliance)
- And other smaller fines, amounting to no more than £700,000

106 Although the *Lladró* case was high profile in nature, it did not result in the OFT imposing a fine. The OFT directed that the offending provisions be removed from the agreements within 20 days, but did not impose a fine. Although it would usually impose a fine for such intentionally anti-competitive behaviour, Lladró had received a comfort letter from the European Commission in respect of the agreements, which *could* be interpreted as implying that the agreements did not restrict competition.

6. Assessment

6.1 Is the national competition act sufficiently taking into consideration the specificity of