



28 September 2009

Unit A2 DG Competition
Antitrust and Mergers Policy and Scrutiny
European Commission
Directorate General Competition
Antitrust Registry
1049 Brussels
Belgium

Ref HT 1171 – stakeholder input

Dear Sir/Madam

Review of the competition rules applicable to vertical agreements

The Association of Licensed Multiple Retailers (*ALMR*) welcomes the opportunity to comment on the Commission's consultation on the revision of the Block Exemption Regulation applicable to Vertical Agreements.

The *ALMR* is the only national trade body in the UK dedicated to representing the interests of pub and bar operators and has restricted its comments solely to the application of the rules in the UK pub sector, and namely the exemption they afford to pub companies, property owning companies and brewers which impose an exclusive purchasing agreement on individuals and small companies leasing property from them. We are uniquely placed to comment on the review of the competition rules having been representing lessees for almost two decades, during which time these agreements have been scrutinised by the EU and UK Competition Authorities.

The *ALMR* works closely with other trade bodies and campaigning groups within the sector and we note and support the representations made by the Campaign for Real Ale, Federation of Small Businesses and Fair Pint. The former represents the interests of consumers and the latter two organisations individual lessees. The *ALMR* in contrast represents the interests of SMEs within the sector.

In addition to our formal response to the consultation, we have appended our most recent representations to the Office of Fair Trading as part of its ongoing investigation of the sector. We hope that this will be helpful by way of background. In light of the OFT investigation, we believe it would be premature for the Commission to state with certainty that the application of the Block Exemption has been positive in respect of the UK pub sector.

We should be happy to provide additional information or to respond directly to any queries you may have.

Yours sincerely

Nick Bish
Chief Executive



REVIEW OF THE COMPETITION RULES APPLICABLE TO VERTICAL AGREEMENTS

OVERVIEW

1. The Association of Licensed Multiple Retailers (*ALMR*) welcomes the opportunity to submit evidence to the European Commission as part of its review of the Vertical Agreements Block Exemption. As the only national trade body dedicated solely to representing the needs and concerns of licensed retailers, and, in this context, leased operators, the Association is well placed to comment on Block Exemption, its application to the UK pub market and the issues raised by it.
2. By way of background, the *ALMR* was formed in 1992 specifically to represent the interests of those companies which own or operate multiple pub estates. Our members are neither landlord nor brewer but small, independent pub operators. Whilst we have a number of national companies within membership, over two-thirds of our members are SMEs operating 50 pubs or fewer under their own branding. As well as pubs and bars, our members also operate food led outlets, clubs and café bars. These are predominantly suburban community or neighbourhood outlets.
3. Currently 98 companies are in membership, between them operating 15,200 pubs and bars – around a quarter of the UK estate. Around a third of the sites within *ALMR* membership will be operated under lease issued by a pub company or other industry landlord. Of these, 73% will operate with an exclusive purchasing agreement as part of the terms of the lease¹. It is this component of our membership which is directly affected by the Commission's determination of the regulation and guidance on the application of the Vertical Agreements Block Exemption.
4. We are concerned that the Commission's provisional conclusion that the existing rules are working well and should not be fundamentally modified fails to take account the problems which have arisen in the UK pub market as a result of its application. We believe that the Commission should review this preliminary conclusion in so far as it relates to the UK pub market as a matter of urgency.

OVERALL FUNCTIONING OF THE CURRENT RULES

5. The Block Exemption Regulation has been in place for almost a decade, but its application to the UK pub market has long been a source of concern and debate. During the 1990s many pub companies applied for individual exemption under then Article 85(3) as there was some concern over whether the general assumption that the tie conferred special commercial and financial advantage to lessees sufficient to outweigh the anti-competitive restrictions contained in the lease agreements could be relied upon.
6. Whilst we believe that the setting out of an overall approach has been helpful in giving businesses certainty, we are concerned that the adoption of a Block Exemption has been interpreted too widely. There has been a general assumption that the Block Exemption confers an automatic legality to all aspects of the agreement regardless of the specific terms of that agreement. Companies issuing leases which include anti-competitive provisions have not carried out the kind of individual assessment of market share, effects and scope of their agreements outlined in the Commission's guidance on the application of the rules.

¹ *ALMR Benchmarking Survey 2009*



7. The assumption within the market has been that the Block Exemption confers absolute legality on the beer tie and therefore the entire agreement between the parties is exempt from any form of scrutiny. We believe that this has led to the exploitation of the Block Exemption by the pub owning companies which has had significant effects on competition in the market, as outlined by CAMRA and ourselves in evidence to the OFT.
8. Since the Block Exemption was last agreed, we have seen the exclusive purchasing agreement systematically extended in terms of scope and effect. The length of tied agreements has been extended over the past two decades from 3-5 year tenancies to the 20-30 year leases favoured by the major national pub companies. In addition, the extent of the exclusive purchasing obligation has been increased from an initial requirement to buy beer to one which now requires the purchase of many ancillary products such as wines, spirits and minerals, gaming machines, insurance etc. In certain instances, we have seen further anti-competitive restrictions being added to the exclusive purchase obligation. For example, in respect of gaming machines, pub owning companies now negotiate up front access payments from machine suppliers. These royalty payments are not shared with the lessee but have the effect of restricting access to the market and also increasing the cost of machine rent to lessees.
9. At the same time, over the past decade there has been significant consolidation within the industry. The number of pub company owned pubs has remained largely stable over the past decade, and now accounts for 27,461 outlets (43.5% of pubs). However, the ownership of these outlets has changed significantly as Punch Taverns and Enterprise Inns have taken over a number of competitors to emerge as dominant players owning around half of these sites. In addition, there has been consolidation in the brewery owned estate, with the emergence of two 'super regional' companies between them operating around half of all brewery-owned leases. Further information on changes in the market is provided in our submission to the Office of Fair Trading which is attached.
10. These factors have combined to create the current problems experienced in the market. The issue of concern is not the existence of an exclusive purchasing obligation per se, but rather the way in which it has been used by certain parties to distort the economic benefit of the parties to the agreement. We believe this has been to the detriment of lessees and ultimately consumers.

PROPOSED NEW REGULATION

11. Clause (5) of the preamble to the proposed new regulation makes clear that "*the benefit of the Block Exemption should be limited to vertical agreements for which it can be assumed with sufficient certainty that they satisfy the conditions of Article 81 (3)*". We do not believe that this can be said with any certainty in this instance.
12. We acknowledge that the existence of market thresholds in the Regulation creates a presumption of safe harbour which means the conditions of 81(3) are likely to be met. Notwithstanding this, we believe it is incumbent upon companies issuing pub leases to carry out an assessment to satisfy themselves that this is the case. We therefore believe that the Commission needs to do more to explain in its guidance how this test is to be applied and what evidence is required to demonstrate that this head is satisfied.
13. The presumption of legality should not be construed as an automatic exemption and it should be made clear that the exemption is for the anti-competitive aspect of the agreement and not the agreement as a whole.



14. The draft regulation and revised guidance make changes to the way in which market share is calculated. We believe that the UK pub market is unique so as to require special guidance on the interpretation of these guidelines in so far as they apply to it. In particular, the market share and de minimis thresholds should be revised downwards to make explicitly clear that agreements which produce anti-competitive effects of the nature identified by CAMRA and the UK Parliament's Business and Enterprise Committee should bear closer scrutiny and should not have the benefit of automatic safe harbour.
15. We note that the Commission is already proposing to reduce the market share threshold for individual companies to 30% and we believe that a corresponding change should be made to the threshold for parallel networks of vertical agreements, such as exist in the UK pub market. In addition, the calculation of market share in the UK pub market should be made by reference to the number of outlets owned or leases issued, expressed as a percentage of the total market. This is because the calculation of market share by turnover is complicated by the fact that the lessee parties are often individual self-employed businessmen rather than publicly quoted companies. In the pub market, turnover is not an accurate assessment of market share or indeed power.
16. Finally, we note that the de minimis threshold is to remain at 15%. We believe that this should be reduced to 5% in the UK pub market.
17. In all of these cases, the Commission must make clearer that these market thresholds are never absolute and that the prohibition of Article 81 (1) can still apply.

WITHDRAWAL OF THE BLOCK EXEMPTION

18. We note that Article 6 and Article 7 provide for the withdrawal of the Block Exemption in certain circumstances – where the effects of the exemption are incompatible with 81(3) or where there is a cumulative impact of parallel networks. It is arguable that these conditions apply to the UK pub market and we would urge the European Commission to liaise with the Office of Fair Trading in the UK to determine whether this is indeed the case.
19. We believe that any revised Block Exemption Regulation and supporting guidance should be strengthened – with the market share threshold for cumulative impact being reduced as per our recommendations above - and make clearer the conditions in which the safe harbour may be withdrawn and the mechanism for so doing.

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Ealing September 2009