



RESPONSE TO THE EUROPEAN COMMISSION REVIEW OF THE COMPETITION RULES APPLICABLE TO VERTICAL AGREEMENTS

The British Beer & Pub Association (BBPA) represents brewing companies and their pub interests, and pub owning companies, accounting for 98% of beer production and around two thirds of the 53,000 pubs in the United Kingdom.

The UK beer and pub industry is complex in that companies are either producers, pub retailers or companies that both brew beer and own pub estates.

The BBPA fully supports the continued operation of the Block Exemption as it stands as this is hugely important to the continued survival of UK brewers and pub operators.

The BBPA fully supports the response of the Brewers of Europe to this consultation.

2. Market share threshold

Article 3 of the Draft Regulation states that:

“The exemption provided for in Article 2 shall apply on condition that the market share held by each of the undertakings party to the agreement does not exceed 30 % on any of the relevant markets affected by the agreement.”

BBPA is seriously concerned about the new definitions proposed for the consideration of market share. Due to the variety of different agreements that exist within the pub sector in the United Kingdom, the proposals could have implications for delivery contracts that are currently in place and which are generally negotiated for a period of five years.

In practice, such a revised approach would lead to a significant level of uncertainty for producers and pub companies. It is often impossible for producers to assess the market shares of other parties with any degree of certainty, particularly if these parties operate on downstream markets on which the producers are not active or which are subject to local particularities which the producers would not be aware of.

In certain defined sectors some market share data may be more easily obtainable, but it would be disproportionate to require an assessment of downstream markets in every situation where the block exemption would apply. In the pub sector, for example, producers will often enter into agreements with pub companies, who will then supply beer exclusively to their 'tied' public houses. Producers will also sell their product exclusively through their own public houses. Market shares for these types of businesses are likely to be assessed on a local level and, in practice, it would be impossible to require producers to conduct a market analysis of each local market. Market share information is unlikely to be available even if geographic markets could be identified.

For example, with over 53,000 pubs in the UK it is possible that a "local market" could comprise several pubs, all located within a small town or village, that are owned by a major pub company but which are run as individual businesses by lessors under "tied" agreements. As such the "local market" might exceed 30%, although unlikely.

Furthermore, this shift in approach is not consistent with the spirit of the block exemption, which is intended to facilitate the implementation of vertical agreements in certain situations without resorting to a full assessment of the impact of these agreements on downstream markets. The Commission retains the option to assess these agreements in greater detail where it perceives a requirement to do so. It would impede the practical commercial advantages of the block exemption to require the parties obtain information which they have no way to verify prior to entering into vertical agreements.

More generally, the impact of the change of approach in the Draft Regulation and draft Guidelines with regards to market share thresholds could disproportionately affect small producers in a variety of sectors in situations where an impact on competition is unlikely.

By way of an example from the brewing sector, this change of approach would unfairly impact the activities of small brewers. In practice, small brewers rely on exclusive beer delivery contracts or other exclusive arrangements to a greater extent than large brewers. Under the existing block exemption, a small brewer can enter into certain restrictive vertical agreements, such as exclusive purchase arrangements, with a certain degree of legal certainty, provided that its market share does not exceed 30%. Under the Draft Regulation and Guidelines however, a small brewer with a negligible market share will not be able to rely on the block exemption if, for example, that small brewer is entering into a vertical agreement with a retailer which possesses a market share of more than 30%. Thus, on the one hand, the Draft Regulation would add an unnecessary element of legal uncertainty to an arrangement which is unlikely to have any significant economic impact; and, on the other hand, the Draft Regulation would impose on the small brewer the requirement to obtain information from the retailer where the small brewer is unlikely to have the resources to verify this information with any degree of accuracy.

However the new requirement would not only have an impact on the activities of the small brewers, but of all brewers (as suppliers) since present agreements which are now exempted might be excluded from the exemption with no more possible way of control by the brewer than simply renouncing to sign contracts with distributors exceeding the 30% threshold in the market of resale.

The proposed change will mean that the scope of the block exemption will be significantly narrower than at present, and many more agreements will have to be specifically assessed under the Commission's Article 81(3) Notice. However, the overwhelming majority of those agreements would not have any effect on competition, and the additional criteria do not, therefore, reflect any economic rationale.

We would therefore submit that the market share thresholds in the current regime should not be modified as proposed.

UK Office of Fair Trading

In support of our view, we would like to refer the Commission to the recently published report from the UK Office of Fair Trading (OFT). OFT have completed a study in response to a complaint from the Campaign for Real Ale (CAMRA), a consumer organisation, about the effect of the beer tie on the market. The report concludes that there is *'no evidence of competition problems that are having a significant impact on consumers'*. It goes on to say that *'there are a number of competing pub outlets owned by different operators and there is competition and choice between different pubs'*.

The report concludes that *'in a competitive market, any strategy by a pub company which compromises the competitive position of its lessees would not be sustainable, as this would in turn be expected to result in sales and margin losses for the lessee and, in turn, for the pub company. To that extent, pub companies' commercial interests would appear to be aligned with the interests of lessees...overall the OFT has reached the view that further investigation of competition problems within the beer and pub market is not warranted.'*

The OFT report demonstrates that there is no market failure as a result of tied agreements and we would submit that since there are no competition issues, there is nothing to be gained in changing the rules which would only result in much time and effort expended for no good purpose.

The entire OFT report can be accessed here:

<http://www.offt.gov.uk/news/press/2009/127-09>

6. Loan provision

Paragraph 143 of the Draft Guidelines states that "The instances of capital market imperfection, whereby it is more efficient for the supplier of a product

than for a bank to provide a loan, will be limited (see efficiency 8 of paragraph 103)".

As the Commission is aware, investments from the brewing sector contribute significantly to the development of businesses in the on-trade segment (so-called "loan-tied outlets"), which largely impact on local community life. Furthermore, whilst such loans are less common in the UK now, in countries which do so, the brewing sector offers financial support for on-trade businesses (bars, pubs, cafés and restaurants) that may have difficulties obtaining equivalent capital injections from banks and other credit institutions in the current economic climate.

This situation is exacerbated by the brewing sector generally possesses better information on on-trade business borrowers and business risk than banks and can often make a more accurate assessment of the reliability of the borrower in question. The vertical restraints which accompany these types of loans often form an adequate commercial justification for the loan where the borrower does not possess the type of security which would be otherwise be required by financial institutions.

For these reasons, the brewing sector considers that its loan-tie arrangements with the on trade segment would fall under efficiency 8 of paragraph 103 of the Draft Guidelines whether or not the loan is regarded as "relationship specific" under paragraph 142.

Conclusions

At the time of its implementation, the current Regulation simplified the existing rules on vertical restraints and, together with the Guidelines, provided suppliers and distributors with essential legal guidance when considering entering into vertical agreements. In the last decade or so since the Regulation came into force, the brewing sector has made a significant effort in order to adapt its vertical agreements to this legislation.

We consider that the Draft Regulation and Draft Guidelines published by the European Commission on 28 July 2009 generally improve on the current regime. However, there are several areas, identified above, where further clarification would be required from the Commission in the interest of legal certainty. As well, as stated above, we believe that changing the current approach to market share thresholds would lead to legal uncertainty, disproportionate requirements on the parties, and unfair adverse effects on brewers of all sizes, but in particular small producers

We consider that the Draft Regulation and Draft Guidelines released by the European Commission on 28 July 2009 generally improve on the current regime. However, as stated above, we believe that changing the current approach to market share thresholds would lead to legal uncertainty, disproportionate requirements on the parties, and unfair adverse effects on brewers of all sizes, but in particular small producers.

We hope that our comments will be helpful to the Commission in highlighting how the current proposals could be improved to the benefit of both the Commission and of undertakings in general in applying the Block Exemption Regulation and its associated Guidelines in future. We have raised several issues which may require further consideration and discussion and we would be more than happy to participate in any further consultations or discussions that the Commission may wish to hold.

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