Walpole Position Paper:

Supporting the luxury industry in the UK

1. Introduction

Walpole welcomes the opportunity to participate in the EU's consultation on the Vertical Agreements Block Exemption Regulation ("VBER")[1] and associated Vertical Guidelines ("VGL"). Walpole previously inputted into the Commission's consultation process leading to the adoption of the existing Vertical Agreements Block Exemption. The subject matter of the consultation is of direct concern to Walpole and its members.

2. About Walpole

Walpole is the official sector body for UK luxury. Founded in 1992 as a not-for-profit organisation, it counts more than 250 British brands in its membership. As the voice of British luxury, Walpole's purpose is to promote, protect and develop a sector worth £48 billion to the UK economy and the jewel in the crown of UK business.

Walpole actively seeks out UK and international business opportunities, promoting growth in the industry through a program of initiatives, including the annual trade mission and press showcase to the US. The UK China Visitor Alliance (UKCVA) has had great success working with Government to make the visa application system simpler, helping bring more Chinese visitors to the UK. As founders of the European Cultural and Creative Industries Alliance (ECCIA), Walpole cements and champions relationships with Europe's luxury and creative sectors.

Dedicated to creating a pipeline of growth for Britain's luxury brands, Walpole also runs the annual mentoring programmes "*Brands of Tomorrow*" a *course in "Luxury Management*" at London Business School and a schools programme, *Future Talent, to promote creative careers to school aged students across the UK.*

3. Our members

Our membership includes a range of businesses who produce a variety of luxury goods. These include both manufacturers and suppliers and retailers present in a diverse range of industries such as fashion & accessories, beauty & fragrance, automotive, food and drink, interiors and furniture. Noted members include Alexander McQueen, Burberry, Church's Shoes, Harrods, Mulberry, Rolls Royce Motor Cars, Wedgwood and Yoox-Net-a-Porter.

In compiling our response, we called upon the experience of our members with the EU rules on vertical agreements and were therefore fortunate enough to able to draw upon a rich bank of knowledge and first hand exposure to the functioning of the rules in practice.

4. The European Luxury Brand Industry

It is important to bear in mind the size, scale and strategic importance of the market for European luxury goods. The global market value of the high-end and luxury industries was equivalent to 5% of European GDP in 2017 (an increase compared to the 4% incidence in

[1] Commission Regulation (EU) No 330/2010 of 20 April 2010, *OJ L 102, 23·4·2010*

2014). If the high-end and luxury industries in Europe were an economy, they would rank as the sixth largest GDP in the European Union[2].

In 2017, the global high end and luxury market was valued at EUR 1.094 billion, having grown by 8% compound annual growth rate ("**CAGR**") since 2014. Many of our own members are drawn in particular from the personal high end luxury goods segment, which accounted for nearly a quarter of the high end and luxury market, with 5% CAGR since 2014.

In 2017, the European high-end and luxury brands employed 2 million individuals directly and indirectly in Europe along the value chain, equivalent to nearly 1% of the total European workforce. The employment generation features of these markets should also not be overlooked. European high-end and luxury industries added 265K jobs in the three years between 2014 and 2017.

5. Distribution and the luxury market

The Commission is well aware already of some of the the key features that set apart luxury goods in terms of the way they are manufactured and sold. In order to preserve their luxury image, certain luxury brands brands must be conveyed through a selective distribution network, that is to say, through authorised distributors. The sales locations of those authorised distributors must comply with a number of requirements relating to their environment, décor and furnishing.

Allowing suppliers of luxury goods to preserve the image and prestige of their products was expressly recognised as having a beneficial, pro-competitive impact in Case C-230/16 of *Coty Germany GmbH v Parfümerie Akzente GmbH* (referred to frequently in our response document as the "Coty judgment"). At paragraphs [24] and [25] of its judgment, the court stated:

"the organisation of a selective distribution network is not prohibited by Article 101(1) TFEU, to the extent that resellers are chosen on the basis of objective criteria of a qualitative nature, laid down uniformly for all potential resellers and not applied in a discriminatory fashion……".

"With particular regard to the question whether selective distribution may be considered necessary in respect of luxury goods, that the quality of such goods is not just the result of their material characteristics, but also of the allure and prestigious image which bestow on them an aura of luxury, that that aura is essential in that it enables consumers to distinguish them from similar goods and, therefore, that an impairment to that aura of luxury is likely to affect the actual quality of those goods".

6. Features of distribution of luxury goods

For many of our members, maintaining the "aura of luxury" around their products depends upon controlling the value chain, the positioning and the presentation of their goods. The distribution chains put in place by our members possess the following key features:

- **consistency of high presentational standards throughout the chain –** maintaining uniform high quality association with a brand means that our members are increasingly making the online and offline sales experience more harmonised,

[2] Statistics in this section are derived from the Bain & Company, 2018 Luxury Goods Worldwide Market Study (2018).

through what has been termed the “omnichannel”. This has the effect of maintaining high standards as well as enhancing brand identity and the consumer experience for both online and offline modes of sale.

- **accessibility of high quality products –** the growing development of omnichannels is testament to another concern of luxury brands, namely ensuring that their high quality goods are available to consumers through a wide range of channels, without compromising on the standards or look and feel of the brand.

- **careful placement and positioning of products** – an attention to detail as to where the products are sold is key to ensure the correct positioning of the product to meet customer expectations. The juxtaposition of luxury and non-luxury goods will taint the perception the consumer has to the detriment of the former.

- **an emphasis on authenticity –** our members are deeply concerned to ensure that the goods which are sold are genuine and that counterfeit goods imitating their genuine products do not infiltrate sales chains. That is not only important to preserve the reputation of their brand but also to avoiding consumer confusion and protecting customers from fraudulent goods of inferior quality. For this reason, for example, one of our members has proposed expressly allowing quantity restrictions on individual orders on internet sales (with a view to restraining bulk sales of goods destined for the grey market)

7. The online challenge and grey market sales

Through our consultation of members, a key concern that permeated feedback related to concerns over online sales. These are clearly seen as a threat to the quality standards which are key to maintaining the luxury image.

The internet improves the accessibility of products as mentioned above but also renders more difficult the ability of brands to place restrictions on where their products are sold. Accessibility is enhanced not only for consumers, which is good, but also for unauthorised re-sellers, which is negative. The fact that goods are frequently sold at a reduced margin online, as well as international price arbitrage, also renders more feasible the purchase and re-sale by unauthorised members of the chain.

That not only presents challenges for suppliers but also creates a “free rider” problem for authorised members of a selective distribution system. They are likely to invest heavily to meet the standards required of the system, only to find themselves undercut by unauthorised sellers, offering the same goods in competition and degrading the brand. That in turn creates a problem for the supplier who may face disaffection from selective distributors and also struggle to find additional or replacement candidates to become authorised re-sellers.

Members are particularly keen to ensure that the rules regarding selective distribution are preserved. They would like to see a codification of the Coty judgment within the Vertical Guidelines. *Coty* has resolved a lot of uncertainty surrounding the permissibility of bands on online third-party platforms.

8. Key concerns of members

It is helpful to summarise here some of the principal concerns expressed by members arising from our consultation with them.

8.1 Need for continuation of VBER and VGL

Those consulted were unanimous in saying that the VBER is generally working well in providing a safe harbour that promotes legal certainty and allows members to build fit for purpose, bespoke channels of distribution with a degree of confidence. Removal of the VBER would create costly legal uncertainty. The VGL are needed as an aid of interpretation of the VBER as well as serving as an authoritative and comprehensive source of previous decisional practice by the Commission and EU Courts.

8.2 Price comparison websites

Members have pointed to the use of price comparison websites as an area of concern. Consumers can be confused and make bad purchasing choices because the basis of the comparison may be misleading (for example because it does not express whether the price displayed is inclusive of taxes). We are aware that in an Opinion of the French *Conseil de la Concurrence* of 2012[3], there was a warning of anti-competitive risks from price comparison websites. These included the display of imprecise or misleading information – a concern that is also held by a number of our members. For these reasons, we would propose a greater ability for suppliers to restrain the marketing of their goods through such websites where this is demonstrably misleading for consumers.

8.3 Brexit

At the current time, the UK's departure from the European Union looms large as a concern in our members' minds.

Members are keen that the two jurisdictions should remain aligned. Although this is not entirely within the Commission's power, the EU-UK political declaration calls for alignment and a level playing field on some issues – and this is such an area where a degree of harmonisation will generate efficiencies and be mutually beneficial. Those consulted were unanimous in saying that post Brexit they do not want to have rules that work for one jurisdiction but not for another.

The Commission can also help by including more guidance on when a restriction on sales outside the EU is likely to be anti-competitive. The decisional practice of the Commission to date appears to have been that such a restriction can cause problems where there is the realistic expectation that the good may be re-imported into the EU from that third state. The UK is even a special case because of the size of the market so some guidance on the situation of restraining exports to the UK may be helpful.

8.4 Inconsistent application of rules on vertical distribution by national courts

Members expressed concern around the divergent application of the rules of distribution in some member states. That was the case for example with regard to some of the states of

[3] Avis n° 12-A-20 du 18 septembre 2012 relatif au fonctionnement concurrentiel du commerce électronique, available at: http://www.autoritedelaconcurrence.fr/pdf/avis/12a20.pdf

Eastern Europe. One member reported that in those states the concept of selective distribution is often not recognised with the result that restrictions are found to be anticompetitive. That member suggested the Commission could take infringement actions against those member states whose courts reached aberrant conclusions. Another – perhaps softer - means of proceeding may be for the Commission to employ advocacy and persuasion with NCAs in the European Competition Network. The Commission could also be more active as an amicus curiae in national proceedings involving the interpretation of EU rules on distribution.

8.5 Active and passive sales

One member commented they think the distinction between active and passive sales could be clearer, particularly in the context of online sales. This can cause issues within a distribution system if an exclusive distributor in one territory considers that a distributor from another territory is encroaching through online sales to customers which have resulted from certain initiatives by the first distributor. It is established for example that simply using the language of a particular member state on a website does not equate to active selling. What if, on the other hand, the distributor advertises on a webpage with a customer specific reference (e.g. "/france" in the domain name). Since the last VGL was issued, there must have been a body of experience which the Commission can draw on and set out in the new VGLs which addresses specific on-line selling practices by distributors which can be usefully classified as active or passive.

8.6 Trade marks

There are a number of areas we have suggested that the Commission could improve certainty and provide additional guidance. One is around trade marks because the guidance in this area is quite short. We would be interested to know, for example, the extent to which it is permissible for an owner of a trade mark licence to impose territorial restrictions on the use of that mark. Again, the Commission could take the opportunity to codify previous decisional practice[4].

8.7 Hardcore restrictions

We would also welcome a slight clarification to the wording of Article 4(b)(iii) of the VABE with regard to the exception on end user restrictions for selective distribution systems (see our response to Question 22).

The current wording is:

"The exemption provided for in Article 2 shall not apply to vertical agreements which, directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object:

(b)the restriction of the territory into which, or of the customers to whom, a buyer party to the agreement, without prejudice to a restriction on its place of establishment, may sell the contract goods or services, except

[4] See for example *Moosehead/Whitbread* OJ [1990] L 100/32

(iii)the restriction of sales by the members of a selective distribution system to unauthorised distributors within the territory reserved by the supplier to operate that system"

This could be read as meaning that the selective distribution can only be defended from the member state in which the distributor or the supplier is based. We think that this should read:

"

(iii)the restriction of sales by the members of a selective distribution system to unauthorised distributors within the territory reserved by the supplier to operate that system or within other territories where the supplier has equivalent selective distributions in place."

This would recognise that selective distribution systems frequently span frontiers and the supplier ought to be able to restrain unauthorised sales into any territory where that system is in operation.

8.8 Multi-tiered distribution

An area of improvement identified by another member related to the creation of multi-tiered distribution systems. A member had wanted to appoint a master distributor who would then find and appoint sub-distributors as part of a selective distribution system. Whilst this is benign and pro-competitive (the master distributor would know the territory and therefore be well placed to find and verify possible candidates), it does not fit easily within the VABE. Is the master distributor to be assimilated to the supplier or to another distributor? The verticals as a whole could be clearer on this point.

8.9 Distribution segmented into different channels

One member also commented that they had struggled slightly with applying the Commission's guidelines to a distribution system where they wanted to assign different channels. This prompted us to review the Commission's guidelines on the feasibility of such a system under the VGL and the definition of "customer groups". Whereas at first glance the Commission says that a customer group can be defined by any objective characteristics, it also seems to suggest that this cannot be done by named customers. It could be clearer on this basis as it may be necessary to provide named customers in order to delineate certain boundaries about who is included within a customer group. It is not clear if this is permitted or not.

9. Supplementary questionnaire response document

We are attaching a further document setting out our responses to the following questions:

- Are the companies/business organisations that are members of your association suppliers or buyers of products and/or services, or both?

- Leaving aside the appropriateness of the scope of the current list of hardcore restrictions (Article 4 VBER) and excluded restrictions (Art 5 VBER) (see the last three questions in this section), do you consider that the additional conditions defined in the VBER (i.e. Article 2 and 3 VBER) lead to the exemption of types of vertical agreements that do not generate efficiencies in line with Article 101(3) of the Treaty?

- Does the list of excluded vertical restrictions (Article 5 VBER) exclude types of vertical restrictions for which it can be assumed with sufficient certainty that they generate efficiencies in line with Article 101(3) of the Treaty?

- Are there any other types of vertical restrictions for which it cannot be assumed with sufficient certainty that they generate efficiencies in line with Article 101(3) of the Treaty but which are not captured by the current list of hardcore restrictions (Article 4 VBER) or excluded restrictions (Article 5 VBER)?

- Please provide an estimate of the possible change in compliance costs – in relation to the question "Would the costs of ensuring compliance of your vertical agreements (or, in the case of a business association, the vertical agreements of the members you are representing) with Article 101 of the Treaty increase if the VBER were not prolonged?"

As the online form did not allow for further comments to be made in relation to the above, we invite the Commission to consider our comments in the supplementary questionnaire response document attached.

10. Follow up

Thank you again for the opportunity of responding to the Commission's consultation process. We remain at your disposal for any further clarification or supplementary information the Commission may require from Walpole.

For and on behalf of

The Walpole Committee Limited