

Lladró Comercial SA

OFT decision of 31st March 2003 By George Peretz

This decision – in which Lladró was found to have infringed Chapter I of the Competition Act but in which no penalty was imposed – raises a number of interesting points.

Facts

In 1999 Lladró – the well known Spanish producer of luxury ceramic figurines – drew up a selective distribution agreement (SDA) which it intended to implement across Europe. It notified the SDA to the EC Commission for negative clearance or exemption. The SDA contained, *inter alia*, a clause that required retailers, before offering discounts on Lladró figurines, (i) to inform Lladró and (ii) to offer the items in question back to Lladró for re-purchase at wholesale price. It also contained a clause that prevented the advertising of discounts.

After discussions between Lladró and Commission officials (in which the clauses referred to were not raised by the Commission), the Commission on 30th March 2000 issued a comfort letter, which indicated that the SDA fell within the terms of the then subsisting Notice on agreements of minor importance (which of course expressly did not cover agreements which had the object or effect of maintaining resale prices) and that it did not have an effect on trade between Member States.

Meanwhile, a number of Lladró retailers had signed the SDA. But for a number of commercial reasons, by March 2000 Lladró had ceased trying to sign retailers up to the SDA. A large number of its retailers never signed it, and Lladró continued to supply them. Those retailers who had signed it were never referred to its terms. In short, the SDA had become a “dead letter”.

In 2000 and 2001 the OFT received complaints from certain Lladró retailers to the effect that supplies had been cut off or restricted because they were discounting resale prices. One retailer covertly tape-recorded a conversation with a Lladró representative in which (according to the OFT) the Lladró representative made comments consistent with that allegation. (Since the OFT would be prevented by the Regulation of Investigatory Powers Act 2000 from instigating that recording, it must be assumed that the retailer arranged the covert recording off his own bat.) Lladró accepted that on occasion it had objected to advertisements which referred to heavy discounting; it submitted that its objection had been to the style of the advertisements, which were inappropriate to a luxury product. It also accepted that it had ceased supplies, or restricted supplies, to certain retailers; that was for reasons other than discounting behaviour (e.g. unsuitable premises).

The restrictions on discounting and advertising of discounts

The decision concentrated on the two clauses of the SDA referred to above. The allegations of Lladró pressure on retailers were relied on as going to confirm the anti-competitive object of those clauses.

The OFT had little difficulty in establishing to its satisfaction that the two clauses had, effectively *per se*, the object of restricting retailers' freedom to set resale prices and hence contravened Chapter I. It did not seriously dispute Lladró's evidence to the effect that by 1st March 2000 (when the Competition Act came into force) the SDA had become a dead letter; but it argued (a) that it could be presumed (despite the lack of any positive evidence to that effect and a significant amount of evidence to the contrary) that the SDA had in the period after 1st March 2000 had some effect on retailers' pricing behaviour; and (b) that even if there had been no effect on competition this was irrelevant because the SDA nonetheless had the *object* of restricting competition. As to this last point, it may be observed that it not entirely obvious that an agreement that had become a dead letter by the time the Competition Act came into force could be said, at any time when that Act was in force, to have had any anti-competitive object.

Anonymous evidence

The identity of four of the retailers on whose evidence the OFT relied was not revealed to Lladró during the course of the administrative procedure. Lladró argued that the OFT should not rely on that evidence. It drew attention to the Strasbourg jurisprudence on the use of anonymous evidence in criminal proceedings, which requires a balance to be struck between the protection of witnesses' legitimate interests on the one hand and the need for the accused to be able adequately to defend himself on the other. It argued that Lladró was unlikely to "punish" retailers when it was under intense scrutiny by the OFT and that the retailers in question were likely to stock a large number of products and were not dependent on Lladró; it also argued that it could not hope to defend itself against allegations based on statements supposed to have been made by Lladró staff without any idea of by whom and to whom those statements were supposed to have been made.

The OFT rejected those arguments. It observed that its administrative proceedings were not required to comply with Article 6. (That is true, but ignores the point that it would be unsatisfactory for the OFT to rely in a decision on material that, because of Article 6, it could not rely on in front of the Competition Appeal Tribunal.) It argued that there were real fears that Lladró might harm retailers who had given evidence to the OFT. It also argued that there was nothing in the anonymous evidence to cast doubt on its credibility. The OFT did not, however, deal with the point that it was impossible for Lladró to test or challenge the credibility of the retailers in question without knowing who they were.

The effect of the Commission's comfort letter

Section 41 of the Competition Act prevents a penalty from being imposed in respect of the period between notification of an agreement to the Commission for exemption under Article 81(3) EC and before "the Commission has determined the matter". The OFT accepted that it was prevented from imposing a penalty in respect of the SDA in the period before the issue of the comfort letter. However, it took the view (without giving reasons) that the comfort letter was a "determination" of the matter, and therefore that section 41 did not apply to the period after 30th March 2000. It has to be said that that conclusion is not as obvious as the OFT makes out. Indeed, the OFT's guide to the Chapter I prohibition (OFT 401) appears to reach the opposite conclusion at §7.11 where it is said that:

*Many agreements notified to the European Commission receive an informal indication of the European Commission's likely assessment by means of a **comfort letter** rather than a formal decision. EC comfort letters are not legally binding but it is clear that the European Commission will re-open the file only in certain limited circumstances. The Act does not*

make provision for the informal procedures of the European Commission. (original emphasis in bold, added emphasis underlined)

And at §6.7 of the OFT's guide to the major provisions of the Competition Act (OFT 400), it is said that immunity lasts under section 41 until the Commission "*formally*" determines the matter.

However, although the OFT maintained that it was not precluded by section 41 from imposing a penalty in respect of the period after the comfort letter was issued, it did accept that it was not right in the circumstances of the case for a penalty to be imposed.

The OFT took some pains in the drafting of the decision to disguise the fact the comfort letter on its face plainly indicated the Commission's view that the SDA fell within the terms of the 1997 Notice on agreements of minor importance; given the terms of that Notice, that entailed a conclusion that the SDA did not have the object or effect of maintaining resale prices (a conclusion that was of course directly contrary to the OFT's view). Instead of quoting the comfort letter itself, the decision rather coyly notes at §§29 and 124 that the Commission subsequently explained (in an e-mail sent to the OFT by a Commission official in 2003) that the decision was issued on the basis that the SDA had no effect on trade between Member States, an *ex post* rationalisation that is in fact somewhat difficult to square with the comfort letter itself.

Nonetheless, the OFT somewhat grudgingly conceded that Lladró could reasonably have been led to conclude that the comfort letter contained a substantive positive competition assessment of the SDA, including the clauses to which the OFT objected, under Article 81 EC. It could therefore reasonably have assumed on the basis of the comfort letter that the SDA was not contrary to Chapter I. On that basis it was not right to impose a penalty on Lladró, although directions were given requiring Lladró formally to amend the SDA to remove the clauses at issue.

**George Peretz and Julian Gregory acted for Lladró before the OFT.
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