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**An examination of the competitiveness of the
methods by which beer has been distributed
in the UK focusing on the beer tie agreement**

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Submitted in fulfilment of the requirements for the degree of PhD.

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Abstract

The thesis seeks to examine the competitiveness of the methods by which beer has been distributed in the UK, particularly the beer tying agreement, with the objective of setting out recommendations for the future. In order to fulfil this objective, the thesis aims firstly to engage in a scholarly exercise of clarifying the role and purpose of the beer tie; the application of the EU competition law provisions to the brewing industry; and the UK Government's approach to regulating it. Secondly, the thesis engages in comparative research and will consider how other non-UK markets have dealt with the distribution of beer, and more specifically the issue of the beer tie. In doing so, the thesis seeks to ascertain how competitive the UK market is in the context of these other geographical markets. The thesis will also compare the UK beer market with another UK market in which the use of tying agreements is prevalent in order to ascertain whether the same issues have been faced in this market as in the beer market. The intention of the comparative research in the thesis is to provide assistance to legal policy makers on the future regulation of beer distribution in the UK. The thesis does not however undertake to propose measures to achieve a state of perfect competition. Rather, it undertakes, as the third aim of the thesis, to propose informed recommendations that address better the on-going anti-competitive concerns associated with the operation of the beer tie today and ensure a socially acceptable level of workable competition.

I declare that, except where explicit reference is made to the contribution of others, this dissertation is the result of my own work and has not been submitted for any other degree at the University of Glasgow or any other institution.

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Competition Act of 3 April 2013

The Establishment of a Competition Authority Act of June 10 2006

The Protection of Economic Competition Act of June 10 2006

Chapter 1 - Introduction

The thesis seeks to examine the competitiveness of the methods by which beer has been distributed in the UK, particularly the beer tying agreement, with the objective of setting out recommendations for the future.

1. Contextual background and motivation for the research

The thesis examines the competitiveness of the mechanisms for the distribution of beer in the UK, focusing on the use of beer tying agreements. The distribution of beer by tying agreements has a very long tradition in the UK market becoming a feature of the UK brewing industry with the emergence of wholesale brewing in the 18th Century.¹ However, as the tie has evolved, this method of distributing beer has also caused concern to successive UK Governments, and has also attracted the attention of the European Union (EU) competition authorities, due to its anticompetitive effects manifested *inter alia* in the closed nature of the trade and lack of price competition between public houses (pubs).

Despite significant intervention by the UK Government in the late 1980s to open up the market to competition, the beer tie has persisted. The scrutinisation of its use has also continued with the rise of the non-brewing pub owning companies (pubcos) over the past twenty-five years.² The on-going operation of the beer tie by these pubcos has been associated with the continuing and significant number of public house closures in the UK, causing this to become an increasingly vexed issue. Whilst the industry is continually changing and consolidating, recent estimates suggest that 58.7% of the UK's pubs are owned and so tied to either a brewer or a pubco.³

Whilst in broad terms the subject matter of the thesis is the competitiveness of the methods by which beer is distributed in the UK market, beer distribution can be broken down into two main channels. The first channel is the off-trade where beer is distributed to retail outlets for consumption off of the premises, such as supermarkets. The second channel is the on-trade, where beer is sold for consumption on licensed premises, namely pubs and on which the thesis is focused. The scope of the thesis is then narrowed further to the competitiveness of tying agreements within the UK on-trade.

¹ The Monopolies and Mergers Commission, *The Supply of Beer A Report on the supply of beer for retail sale in the United Kingdom* (Cm651, 1989) at para 2.1, p6

² Brewing pubcos exist in the UK market but are fewer in size and number than their non-brewing counterparts

³ As at 2012. R Hucker, (ed), 'Market Report 2013, Public Houses' (Key Note, 2013) at Table 2.4, p21

In 2010, at the beginning of the thesis, whilst I was working for the international brewer Heineken, the pressure group the Campaign for Real Ale (CAMRA), as a designated consumer body, had made a much publicised ‘super-complaint’ to the then UK competition authority, the Office of Fair Trading (OFT)⁴ concerning the UK pub industry. In accordance with s.11 of the Enterprise Act 2002, such a complaint is permissible where a designated consumer body believes any feature, or combination of features, of a market in the UK for goods or services is, or appears to be, significantly harming the interests of consumers. Whilst unsuccessful, with the OFT ruling that it had ‘not found evidence of any anticompetitive problems that are having a significant impact on consumers’, the issue of the use of the beer tie has persisted, as it did for decades prior to the Super Complaint.⁵

Consequently since the research began, there have been numerous additions to the existing and vast body of Government backed reports into the issue of the beer tie. However, despite the question of the competitiveness of UK beer tie agreements not being an entirely novel one, with much research already being produced on this topic, it is apparent that there is a gap in the literature that the thesis looks to fill. Whilst the existing body of work serves to highlight the importance and significance of the subject matter, the vast majority of literature on the distribution of beer in the UK is not academic literature, although a body of such literature does exist. Rather, the literature has been produced by interested parties such as Government backed Departments and Committees as well as pressure groups. Further, despite over a decade of declining to intervene in the operation of the beer tie, following its intervention in the late 1980s, on 26th March 2015 the Small Business Enterprise and Employment Act received Royal Assent (2015 Act). Part 4 of the 2015 Act introduces a statutory Pubs Code for England and Wales,⁶ along with an independent Pubs Code Adjudicator to enforce it. Thus, this is an opportune moment to examine critically the role of tying agreements in the distribution of beer in the UK and to evaluate whether statutory regulation is the correct solution to the competition problems that have arisen in the UK beer distribution market. Consequently, the key objective of the thesis, in contrast to the existing body of work on this topic, is to provide an objective, systematic and holistic analysis of the issue.

In doing so, the thesis aims firstly to engage in a scholarly exercise of clarifying the role and purpose of the beer tie; the application of the EU competition law provisions to the brewing industry; and the UK Government’s approach to regulating it. Having analysed its

⁴ As of 1st April 2014 the OFT closed with its responsibilities passing to the Competition and Markets Authority however for simplicity it will be referred to throughout the thesis as the OFT.

⁵ Office of Fair Trading, *CAMRA super-complaint – OFT final decision* (OFT 1279, 2010) at p6

⁶ This is a devolved matter however similar intervention is being considered in Scotland.

role, purpose and regulation, the thesis will engage, secondly, in comparative research and will consider how other non-UK markets (United States, Australia and Belgium) have dealt with the distribution of beer, and more specifically the issue of the beer tie. In doing so, the thesis seeks to ascertain how competitive the UK market is in the context of these other geographical markets, whilst acknowledging the limitations of such international comparison. The thesis will also compare the UK beer market with another UK market (petroleum) in which the use of tying agreements is prevalent in order to ascertain whether or not the same issues have been faced in this market as in the beer market. The intention of the comparative research in the thesis is to provide assistance to legal policy makers on the future regulation of beer distribution in the UK. Whilst the complex legal, historical and economic issues specific to the UK market have long proven stumbling blocks in the search for the perfect solution to the issues faced, the thesis does not undertake to propose measures to achieve a state of perfect competition. Rather, it undertakes, as the third aim of the thesis, the more modest task of proposing informed recommendations that better address the on-going anti-competitive concerns associated with the operation of the beer tie today and ensure a socially acceptable level of workable competition.

2. The research questions

The main objective of the thesis is to examine the competitiveness of the methods by which beer has been distributed in the United Kingdom (UK), focusing on the beer tying agreement, with one primary objective of setting out recommendations that better address the on-going anti-competitive concerns associated with the operation of the beer tie today and ensure a socially acceptable level of workable competition. The six main research questions to comply with this objective are as follows.

- 1) Given the historical development of the beer market in the United Kingdom, why has the beer tie been such an integral part of its development up to and including the 21st Century?
- 2) Given that the EU has a strong competition law regime to open up markets to competition, with tying agreements having the opposite effect, how have the EU competition law rules been applied to the brewing industry which relies on the use of such agreements?
- 3) How has the United Kingdom Government regulated the beer tie?

- 4) How have other geographical markets, such as the USA, Australia and Belgium, dealt with beer distribution?
- 5) Have other markets that rely on tying agreements, such as the petroleum market in the United Kingdom, had the same issues as the distribution of beer in the United Kingdom?
- 6) What reforms are required to the distribution of beer in the United Kingdom?

3. The methodology and sources

As stated previously, the thesis is concerned with the competitiveness of the methods by which beer has been distributed in the UK, particularly the beer tying agreement, and with proposing recommendations for the future. Research therefore began with a consideration of the historical development of the beer market in the UK to determine the role of the beer tie. This necessitated a literature review of historical works on the UK brewing industry, the development of the tied house system, industrial organisation and the history of liquor licensing in this country. However, as was to be a recurring theme throughout this research process, given the on-going interest of successive Governments in the operation of the market, comprehensive reports produced by various Government bodies up to the year 2000, have also been reviewed. These provide an overview of the competitive situation prevailing in the UK market as at the date of publication and the primary concerns and issues that required to be addressed. The terms of statutory instruments implemented to address the concerns identified in the foregoing reports over the use of the beer tie are also considered and the implications of such measures for the market are reviewed. In doing so, market reports on the operation of the beer and public house markets provided valuable insight into market size, competitor analysis and market forecasts at different points in time, thereby assisting in developing an accurate representation of the market, as did the relevant academic literature on the operation of beer tie agreements in the UK and the effects of Government intervention in the market.

The thesis also draws on the application of the EU competition law rules, particularly Article 101 Treaty on the Functioning of the European Union (TFEU), to tying agreements. However, at the EU level, the study focuses not only on the primary Treaty provisions, but also considers in detail the provisions and application of successive vertical agreement block exemption Regulations (BER). The case law of the Court of Justice of the European Union (CJEU), the General Court and the European Commission dealing with the interpretation and application of the EU competition rules to vertical agreements, and

more specifically beer tying agreements, has also been reviewed. This has been instructive in charting the evolving approach of the EU in the application of these rules to the brewing industry. Numerous Commission Notices on the application of the Treaty provisions and the BERs, as well as Commission Guidelines and Reports on competition have been relied on in this regard. Several standard literature works on the EU and on the economic effects of vertical agreements⁷ have been reviewed in conjunction with academic works dealing specifically with the issue of the beer tie.⁸

The thesis then explores how the UK Government has regulated the beer tie, noting the influence the EU has had on its approach since the UK's accession in 1973. This necessitated that the relevant case law of the UK courts on the issue of the legality and application of the beer tie be reviewed. The UK legal regime and its harmonisation with the EU competition law provisions have also been investigated, thereby necessitating a review of the UK competition law regime applicable to beer tying agreements. In charting the concerns over the use of the beer tie since the year 2000, and the UK Government's response to those concerns, again the reports produced by the UK Government and associated bodies have been reviewed, most notably those of the Trade and Industry Committee, the Department of Business Innovation and Skills and its Committee, as well as the OFT. The CAMRA super complaint is also reviewed in order to further understand the on-going concerns over the operation of the beer tie in the UK. In light of the very recent enactment of the 2015 Act, in order to inform a critical analysis of its provisions, Hansard has been consulted to ascertain Parliament's motivations behind Part 4 of the Act.

After considering the EU and UK positions on the use of beer tying agreements, the thesis then considers how other geographical markets have dealt with the distribution of beer. This is in order to ascertain whether any guidance can be gleaned as to appropriate future recommendations for the UK. Following a review of general texts⁹ on other geographical markets, three jurisdictions were selected for comparison on a case study basis. Firstly, the United States (US) as it is one of the largest and most established beer markets but has long outlawed the use of the beer tie; secondly, Australia as it is a Commonwealth country

⁷ For example J Goyder, *EU Distribution Law* 5th Edition (Oxford, Hart Publishing, 2011); A Jones and B Sufrin, *EU Competition Law Texts, Cases and Materials* 5th Edition (Oxford, Oxford University Press, 2014); S Marco Colino, *Vertical Agreements and Competition Law A Comparative Study of the EU and US Regimes* (Oxford, Hart Publishing, 2010); and V Korah and W.A. Rothnie, *Exclusive Distribution and the EEC Competition Rules Regulations 1983/83 and 1984/83* 2nd Edition (London, Sweet and Maxwell, 1982)

⁸ For example, I.M. Sinan, 'Tied House Agreements and the EEC Competition Rules: A Brief History' (1985) N.L.J. 25 October 1063; and D.A Everreste, 'British and European Community regulation of the British Beer Market: Tapping into the tied house system (Cheers!)' (1990) 20 Ga. J. Int'l & Comp. L. 583

⁹ For example J.F.M. Swinnen, eds, *The Economics of Beer* (New York, Oxford University Press Inc., 2011); D Kirkby et al, *The Australian Pub* (Sydney, UNSW Press, 2010); and A Mittelman, *Brewing Battles a History of American Beer* (United States, Algora Publishing, 2008)

which recently implemented measures to outlaw the use of the beer tie subject to certain exceptions; and thirdly, Belgium which is another EU Member State which permits the use of the beer tie but is considered to have one of the most diversified beer markets in the world. The investigation of these markets required a review of historical texts on the evolution of each beer market in order to determine how their development has influenced their current day market structures and the means employed to distribute beer. The evolution of the competition law regime in each jurisdiction was also investigated through consideration of the relevant statutory provisions, and in the US the provisions of the US Constitution were considered. Literature on the current day market structures and competition law regimes in all three jurisdictions was subsequently reviewed. However, certain restrictions were imposed on the investigation into these markets. With regard to the Belgian beer market language limitations were encountered as Belgian legislation and cases are officially translated into Dutch and French only and literature on the historical development of the market and on its wholesale sector is largely in these languages. This limited the sources available to draw upon causing reliance to be placed on only a relatively limited number of sources. More generally, a further limitation on the research was presented by the difficulty experienced in obtaining accurate and up to date statistics on the brewing markets in each of these jurisdictions. The most comprehensive information is confined to market reports produced by independent providers of strategic market research, and these have not been accessible in the course of this research. Reliance has therefore had to be placed on alternative sources that are potentially not as detailed.

The thesis then considers whether another market in the UK that also relies heavily on tying agreements, namely the petroleum market, has also faced the same issues as the brewing industry. Comparing the distribution of beer and petrol required a review of the historical development of the petroleum market in order to understand the role of tying agreements within it and to ascertain the current day market structure. This necessitated consideration of market reports and historical reports produced by Government bodies such as the Monopolies and Mergers Commission (MMC). The numerous similarities between these two markets have also been recognised at the EU level meriting special treatment for exclusive purchasing agreements within these industries under the EU competition law provisions. Consequently, the relevant provisions of the EU BERs were considered. The research sources for these markets therefore also share many similarities. As with the UK beer market, there have been numerous and on-going Government investigations into the operation of the UK petroleum industry and so consideration of this market required that these be reviewed in order to identify any similarities with the

concerns associated with the distribution of beer. This also provided an insight into the structure of the market at various points in time, up to and including the current day, the competition issues raised and the Government's response.

Finally, the thesis makes recommendations for the reform of the distribution of beer drawing on the preceding chapters.

4. The structure of the thesis

The thesis is divided into 7 main chapters, each seeking to provide answers to the research questions. Chapter 1 sets out the objectives, research questions and the structure of the thesis.

Chapter 2 establishes the historical links between the British brewing industry and public houses, helping the reader to understand why the beer tie has been and continues to be an integral part of the UK market. It identifies the growing concerns of successive UK Governments over the use of such tying agreements up to the year 2000 and analyses the action taken to open up the market to competition by the UK Government.

Chapter 3 examines the application of the EU competition rules to vertical tying agreements with particular emphasis on the distribution agreements for beer. This Chapter provides a contextual background to the EU's evolving approach towards such vertical agreements, and to the EU BERs which now play a central role in the application of the EU competition rules to such agreements. The EU's stance on these agreements also has its roots in the unique goals of EU competition law and in the seminal case law of the European Commission and the CJEU which is considered in the chapter.

Chapter 4 follows with an analysis of the UK Government's policy on the regulation of beer tying agreements. This provides an insight into the evolution of the UK's approach towards these agreements. The chapter considers the UK's accession to the EU and reviews the harmonisation of the UK's competition law regime applicable to beer tying agreements with the European rules. The numerous reports resulting from on-going enquiries into the UK market from the year 2000 onwards are also reviewed noting any influence the EU's position has had on the UK Government's tolerance of these arrangements. Finally the chapter critiques the provisions of Part 4 of the 2015 Act, which addresses the use of beer tying agreements in the UK market.

Chapters 5 sets out by way of comparison with the US, Australia and Belgium whether any guidance can be gleaned from other non-UK beer markets when making recommendations

for the future reform of beer distribution in the UK. The evolution of these beer markets and the legal regimes regulating them will be analysed as part of this selective comparison. In this chapter it will be concluded whether or not these regimes provide a solution to the issues faced in the UK over the use of beer tying agreements.

Chapter 6 then follows with an analysis of the petroleum industry in the UK, as this is an industry in which tying agreements are also widely used and which shares certain characteristics with the UK beer market. This Chapter will ascertain whether or not the UK petroleum industry has encountered the same issues as the distribution of beer in the UK and whether it provides any guidance regarding the future regulation of beer distribution in the UK.

Finally Chapter 7 draws on the foregoing chapters and details the conclusions of the thesis and proposes recommendations for the reform of beer distribution in the UK.

The cut-off date for the research is 26th March 2015.

Chapter 2 - The UK's Beer Distribution Market

This chapter maps the historical development of the beer market in the United Kingdom with the objective of understanding why the beer tie agreement has become such an integral feature of the UK market right up to and including the 21st Century. The chapter also considers the anticompetitive concerns of such agreements which prompted unprecedented Government intervention in the form of the Beer Orders in 1989.

The chapter first provides a brief description of the history of the beer distribution market in the UK and, in particular, examines the links binding the British brewing industry with the public house market (Subsection 1). The focus of the chapter then turns to the anticompetitive concerns that have worried successive UK Government and competition authorities, resulting in an investigation by the Monopolies and Mergers Commission (MMC), the issue of the Beer Orders, and the subsequent emergence of pub companies (pubcos). The position is reviewed to the point of the OFT's decision to revoke the Beer Orders in 2000 (Subsection 2).

1. A brief historical context: the links binding the British brewing industry to the public house market

The British brewing industry has long been linked to the public house market with both sharing a great history spanning back as far as Roman Times.¹ This vertical integration between the production and retailing of beer has therefore been a characteristic of the industry for a long time, with wholesale brewing developing in the eighteenth century. However, Government intervention, for non-economic reasons, through licensing laws and regulations, has also affected its structure, with the licensing of local ale houses being introduced in 1552.² This invariably tightened and relaxed over the subsequent decades as the brewing industry evolved through periods of varying degrees of hostility. These ranged from the temperance movement to latter day public interest concerns. However, it was in the eighteenth century that the custom which came to be known as the 'loan tie' emerged.³ The loan tie hugely influenced the retailing of beer by allowing the brewer to maintain

¹ The Monopolies and Mergers Commission, *The Supply of Beer A Report on the supply of beer for retail sale in the United Kingdom* (Cm651, 1989) at para 2.1, p6

² Ibid at para 2.1, p6. Regulation of the trade in alcohol was considered necessary as "free use of intoxicating drinks produced not only incapacity and disease among all classes but also...idleness and disorderly living, crimes against life and property and even riot and rebellion." S Webb and B Webb, *History of Liquor Licensing in England Principally from 1700 to 1830* (London, Longmans Green & Company, 1903) at p2

³ K.H. Hawkins and C.L. Pass, *The Brewing Industry A Study in Organisational and Public Policy* (London, Heinemann Educational Books, 1979) at p18.

control over the products sold in retail outlets in exchange for a loan to the licensee.⁴ Further, the property tie, whereby licensed houses are owned by brewers and leased to tenants on the provision that only the Landlord's beers are sold on the premises, was later to emerge towards the end of the nineteenth century.⁵ The property tie has been, and continues to be, as controversial today. Consequently, public and Parliamentary concern over the relationship between the brewer and the licensee has been on-going since the nineteenth century.⁶

Nevertheless, it should be noted at the outset that varying approaches, and degrees of control, were exerted by brewers in different parts of the country at different times.⁷ This is best exemplified by the Scottish market where, as will be discussed below, the licensing laws were very different from those in England, and so, the tied house system was largely unknown in Scotland as late as 1914, with free houses continuing to dominate for years after.⁸ London, however, emerged in the early eighteenth century as the centre of commercial brewing, and so it will primarily be used to illustrate the evolution of the beer tie by way of loan and property ownership.⁹

1.1 The emergence of wholesale brewing

In charting the evolution of the beer tie and the brewing industry, Vaizey states “[o]ne of the most consistent trends in the history of brewing in the nineteenth century was the decline of the small brewers and the gradual concentration of beer output on the bigger breweries”.¹⁰ This was due to the fact that during the eighteenth century, the brewing process was relatively primitive.¹¹ It was a primarily domestic industry, dominated by publican brewers producing beer either for their own consumption or for sale on their premises.¹² Donnachie notes that in Scotland, brewing remained a largely domestic activity until the late eighteenth century with brewing publicans not being uncommon in the early

⁴ Above n.1, at para 2.1, p6 and above n.3 at p18

⁵ D.M. Knox, ‘The Development of the Tied House System in London’ (1958) 10 Oxf Econ Pap 66 at p66

⁶ Above, n.1 at para 2.1, p6

⁷ Above, n.5 at p67

⁸ T.R. Gourvish and R.G. Wilson, *The British Brewing Industry 1830-1980* (Cambridge, Cambridge University Press, 2008) at p409

⁹ In outlying areas commercial brewing developed in the central industrial areas and in particular Burton-on-Trent, where Bass and Allsopp dominated the trade as the water was particularly suited to certain types of beer and attracted many large brewers. A Seldon, ‘The British Brewing Industry’ (1953) (October) Lloyds Bank Review 30 at p31

¹⁰ J Vaizey, *The Brewing Industry 1886-1951 An Economic Study* (London, Sir Isaac Pitman & Sons Ltd, 1960) at p3

¹¹ Above, n.3 at p14

¹² Ibid at p14

nineteenth century.¹³ Large commercial brewers failed to displace smaller regional brewers in Scotland until 1850-1914, whilst in England this process was already under way.¹⁴

Wholesale brewers, meaning those who brewed beer at one location and distributed it to other retail outlets, appeared in the eighteenth century.¹⁵ Brewing was at the forefront of the retailing revolution which saw the majority of trade in London and larger towns being done on a substantial scale at designated points of sale.¹⁶ Further, at this time there were significant and highly important differences in regional and local tastes and the competitive character of the brewing industry was focused on the strength, flavour and reliability of the brewer's products.¹⁷ Consequently, 'porter', a heavy brew preferred in London, had a significant impact on the organisation of the London trade.¹⁸ It could be brewed in very large quantities and resulted in the concentration of brewing amongst a dozen large brewers, who gained significant cost, as well as quality, advantages due to the scale of their operations.¹⁹ Further, as retailers increasingly opted to obtain the bulk of their supplies from a single brewer, this development enabled the brewer to judge demand for his product. Such a steady demand was essential in order to ensure economic production as beer is a perishable product.²⁰ Consequently, Mathias suggests that from the end of the eighteenth century, brewers intentionally sought to gain control of the retail trade.²¹

From 1790 onwards, with the re-introduction of restrictive licensing, for the brewer, the economic significance of the reliant publican increased and there was a drive to obtain tied trade. Mathias states that there is evidence from early in the eighteenth century suggesting that public houses were also increasingly falling into the possession of brewers through bankruptcy and 'accidents of trade'.²² Consequently, he suggests that "the tied house was universal, and co-extensive with wholesale brewing: it may well have been coeval with

¹³ I Donnachie, *A History of the Brewing Industry in Scotland* (Edinburgh, John Donald Publishers Limited, 1979) at p117

¹⁴ Ibid at p160

¹⁵ Above, n.1 at para 2.1, p6

¹⁶ By 1880, the industry was increasingly concentrated amongst larger enterprises which were able to reduce their unit costs at a faster rate than the smaller brewers. (Above, n.10 at p4 and p6) Vaizey notes that as the brewing process became more exact as the industry became more scientific, the optimum size of breweries increased and the available market area also grew due to advances in transportation. (See above, n.10 at p6)

¹⁷ Above, n.3 at p19

¹⁸ Ibid at p19

¹⁹ Ibid at p19. At later dates, the same concentration occurred in Bristol, Burton-on-Trent, Norwich and Dublin as wealthy individuals maximised the economies of scale made possible by the technical advancements. Above n.10 at p3

²⁰ Above, n.5 at 67

²¹ P Mathias, *The Brewing Industry in England 1700-1830* (Cambridge, Cambridge University Press, 1959) at p119

²² Ibid at p119

it.”²³ However, despite this evidence, tied houses did not absorb large amounts of capital and the brewer was rarely the freeholder of the houses under his control, often making a loss, not a profit, in his capacity as landlord.²⁴ Consequently, from the outset it was apparent that this investment was not made with a view to profiting in the real estate market, but rather to further the brewer’s interests as a brewer.²⁵

1.2 The impact of restrictive licensing

However, despite the weight afforded by Mathias to wholesale brewing as a reason for the development of the tied house system, the structure of the brewing industry has also long been affected by state intervention on public interest grounds. This has principally been by way of licensing as a reaction by the UK Parliament to drunkenness and with the control of the licensing process being conferred on the Justices of the Peace due to its association with the prevention of crime.²⁶ Consequently, Knox supports the view of S and B Webb that the foundations of the close relationship between the brewing industry and retail outlets were strengthened as restrictive licensing highlighted the logic of vertical integration.²⁷ Brewers sought greater control of retail outlets in 1790 when restrictive licensing was enforced, following on from a period of leniency which had been largely unrestricted until 1787.²⁸ This came to an end as concern grew over the ever rising number of beer and ale houses as well as the “*unruly and rowdy*” behaviour of the clientele.²⁹ Legislation was subsequently introduced which afforded Justices of the Peace great power in reducing the number of licences available, whilst also permitting them to exercise tighter control of the remaining licences.³⁰ This included refusal of new licences, the withdrawal of licences where the public house was not properly conducted, and in some cases, the introduction of local veto regarding the opening of new public houses and the closing of existing ones without any compensation.³¹ Consequently, S and B Webb explain the need

²³ Ibid at p120

²⁴ Often the brewer had to make payments to the freeholder which almost rivalled the rent received, and was responsible for the upkeep of the property. (Ibid at p120)

²⁵ Ibid p120

²⁶ Although beer was once “*regarded as a necessity of life*”, enjoyed with every meal and preferred by the majority of the population, S and B Webb state that due to the crime and nuisance associated with excessive drinking, successive governments have been forced to tackle the cause, and so have brought the trade in alcohol under legislative regulation. S Webb and B Webb, *History of Liquor Licensing in England Principally from 1700 to 1830* (London, Longmans Green & Company, 1903) at p 2-4

²⁷ Above, n.5 at 66. This is also supported by Hawkins and Pass. Above, n.3 at p3

²⁸ Above, n.3 at p17. As S and B Webb note, during this period, licences to keep ale houses could be issued by two Justices of the Peace, regardless of whether they had any knowledge of the applicant and effectively were granted to anyone and not withdrawn. Above, n.26 at p15

²⁹ Above, n.3 at p17

³⁰ Above, n.3 at p17. The Monopolies Commission, *Beer – A Report on the Supply of beer* (HC 1969, 216) at p153-158

³¹ Above, n.26 at p49-50

for and intensification of ownership and control of retail outlets at such an early stage within the licensed trade on the basis of restrictive licensing. They noted discontent over tying between 1816 and 1830 but considered that greater stringency in the licensing process encouraged the practice.³²

*“When Justices made it a practice, before granting a licence, to require that the applicant should show that he occupied premises suitable for the business, they insensibly passed into virtually licensing the houses, as well as the particular occupiers. It then became inevitable that the brewers, commanding large capitals, should advance money to enable the necessary alterations to be made, and thus obtain control of a large proportion of the premises on which drink was sold, either by simple purchase of the property, or by the publican’s indebtedness. It was reiterated on all side, that limitation of the number of public-houses, their alteration and enlargement to suit the requirements of the Justices, the insistence on substantial sureties for good behaviour, and the general increase of pecuniary responsibility involved in stricter regulation, all fostered the tied house system.”*³³

Consequently, it is clear that restrictive licensing had a significant role to play in the initial development of the loan tie. This practice of loan tying was established throughout England by 1817, when the Select Committee reporting on the conditions in the trade, noted that approximately one half of London public houses were tied and that the practice was also prevalent in country areas.³⁴ By contrast, Donnachie states that evidence of tied trade in Scotland before 1850 is very limited with none of the existing brewery archives providing any evidence of this.³⁵

1.3 The loan tie and its advantages

For the reasons stated above, the loan tie was extensively utilised by the London brewers. The restrictions on the number of licences available gave rise to what was known as a “*monopoly value*” and thereby encouraged the development of this practice of loan tying.³⁶ Due to the significant level of investment required to acquire such a property, which was greater than that commonly available to those wishing to enter the retail trade, potential publicans were forced to obtain loans in order to finance such entry.³⁷ Knox comments that

³² Ibid at p88

³³ Ibid at p88-89

³⁴ This was the Select Committee of the House of Commons on Public Breweries, 1817. Above, n.3 at p26-27

³⁵ Above, n.13 at p128

³⁶ Above, n.5 at p67

³⁷ Ibid at p67

brewers were virtually the sole source of such funding.³⁸ This was due to the precarious nature of such lending, on account of the insecurity of the licence obtained, which could be removed at any time by the Licensing Justices on the grounds of misconduct.³⁹ This consequently precluded the possibility of obtaining funds from any sources other than brewers who obtained a trading advantage from the arrangement.⁴⁰ The brewers were also eager to secure a degree of control over the licensee in order to avoid the potential loss of their investment.⁴¹ Consequently, as Girouard notes the system operated on the basis that a publican wishing to acquire a public house would borrow a significant proportion of the money required to do so from the brewer, on which he would pay interest and agree to buy the brewer's beer.⁴² The agreement was not binding and in the event the publican bought beer from another brewer, the loan would be called in.⁴³ Consequently, although this was a risky strategy as the value of the public house depended on a licence being in place, brewers were prepared to take the risk.⁴⁴ This was due to the interest paid and the assurance of a guaranteed outlet for their beer.⁴⁵

Subsequently, brewers' considered the advantages of the tie to outweigh the disadvantages. They held the entire trade of each tied publican, thereby creating a constant demand for their product. This enabled the brewer to estimate sales of his products more accurately than was possible in a free market, at a time when he was under an obligation to take back any beer that went unsold.⁴⁶ This was also useful as beer's perishable nature precluded stock piling, and so, the tie assisted with planning, production and storage.⁴⁷ Such constant demand was also of importance in ensuring economic production as brewing has always been a scale economy. Brewers had to utilise their full capacity in order to keep costs at an acceptable level, thereby further driving the brewer's desire to control as many public houses as possible, often within sufficient proximity to the brewery to minimise transportation costs.⁴⁸ However, brewers were also keen to gain control of the retail side of the market, as facilitated by the beer tie, given that increasing importance was attached to reputation and branding. Vaizey states that "[b]eer was perishable and had to be handled

³⁸ Ibid at p67

³⁹ Ibid at p67

⁴⁰ Ibid at p67

⁴¹ Ibid at p67

⁴² M Girouard, *Victorian Pubs* (London, Yale University Press, 1984) at p89

⁴³ Ibid at p89

⁴⁴ Ibid at p89

⁴⁵ Ibid at p89

⁴⁶ Above, n.21 at p123-124

⁴⁷ Above, n.5 at p67 and above, n.21 at p123-124

⁴⁸ Above, n.10 at p140

carefully because bad handling could ruin the reputation of the product”.⁴⁹ Consequently, numerous advantages were presented to the brewer by tying the retail trade, although concern was subsequently expressed over its foreclosure effects on the market.

1.4 Early concerns regarding the competitive impact of the tie

The 1817 Select Committee expressed concerns that this practice of tying public houses to such exclusive dealing arrangements made trade too closed.⁵⁰ However, a more relaxed approach to licensing was advocated by the Committee with this being acted on by the Justices of the Peace.⁵¹ The Select Committee considered that the ‘most objectionable feature’ of the monopoly held by the English brewers by virtue of the tie was “*the restricted power which the public at large possess of employing their capital in the trade of victualing houses*”.⁵² Further, Members of Parliament from 1816 to 1830 were also concerned with the anticompetitive impact of the practice, with it being noted that the main brewers of the time gathered and ‘fixed the price of porter’.⁵³ They also highlighted that the grant of a licence caused the value of the property to rise exponentially as well as the price of beer sold from it.⁵⁴ Consequently, measures were ultimately introduced to create ‘free-trade’ in beer⁵⁵ and from 1830 to 1869 there was a relaxation in the licensing laws through the enactment of the Beer Act 1830.⁵⁶ Beer licences were issued on payment of only a small duty to the Excise Offices, a move which has been credited with fuelling the beer boom of the 1830-1869 period.⁵⁷ The intention had been to create a new form of drinking establishment, free from the control of both Justices of the Peace and commercial brewers. Naturally this resulted in the rise of the new ‘beerhouse’ as well as public houses,⁵⁸ although Vaizey states there is no evidence to suggest that this resulted in a decrease in the number of tied houses.⁵⁹ This was due to the fact that, in contrast to the restricted licences prior to 1830, little value was placed on these licences which were

⁴⁹ Above, n.3 at p26 citing J Vaizey, *The Brewing Industry 1886-1951 An Economic Study* (London, Sir Isaac Pitman & Sons Ltd, 1960), at (sic) p400

⁵⁰ Above, n.3 at p17-18

⁵¹ Ibid at p17-18

⁵² Above, n.26 at p91. Committee on the state of the Police of the Metropolis, *First Report from the Committee on the State of the Police of the Metropolis: with Minutes of evidence taken before the Committee* (HC 1817, 233) at p10

⁵³ Above, n.26 at p92 citing Hansard 1st May 1818

⁵⁴ Above, n.26 at p92-93

⁵⁵ The Chancellor of the Exchequer took the decision in 1830 to end the tax on beer and cider and to take measures to fully open trade. (Above, n.26 at p113). Two measures were introduced. The first was the abolition of tax on beer and the second was the Beer Act 1830 which enabled tax payers to sell beer from their premises without the necessity of obtaining a Justices’ license. (Above, n.3 at p18)

⁵⁶ Above, n.10 at p6

⁵⁷ Above, n.10 at p6

⁵⁸ Above, n.3 at p18

⁵⁹ Above, n.10 at p6

frequently abandoned.⁶⁰ The publicans' dependence on commercial brewers however persisted as the higher prices of public houses caused by the licence premium continued to force publicans to seek financial assistance from brewers. Consequently, according to Vaizey, this perpetuated the exclusive dealing arrangements that already existed during the restrictive licensing era.⁶¹

1.5 The return to restrictive licensing and declining market conditions

The rise of the temperance movement saw various parliamentary committees investigate the beer trade and confirm the problems of uncontrolled drinking. However, in light of the problems previously caused by restrictive licensing and the subsequent drive to tie houses, the re-introduction of licensing did not occur until 1869, in the form of the Beer and Wine Act.⁶² This again forced brewers to be even more concerned with the retail trade than they had been previously.⁶³ By limiting the number of licensed houses, this again created a scarcity value. This ultimately forced brewers to acquire public houses in order to guarantee outlets to supply and thereby encouraged the spread of the tied house system.⁶⁴ Brewers' feared exclusion from the market as their competitors sought to tie remaining public houses, and thereby caused an almost instantaneous increase in property values and forced publicans to continue to seek financial assistance from brewers.⁶⁵ However, in the years following 1870, there was increasing hostility towards the drinks trade as the temperance movement gathered greater momentum and beer consumption declined and remained at a lower level throughout the 1880s.⁶⁶ Consequently, Hawkins and Pass state that the role of restrictive licensing in driving the growth of the tied trade should not be over-stated and the primary push to tie trade was ultimately the reduced market demand and a subsequent increase in competitive pressures.⁶⁷ Nevertheless, both the declining demand and the re-introduction of restrictive licensing, were influential in the growth of the tied house system at this time.

Moreover, over this period, brewers were lending increasing sums of money to publicans due to inflated property values and to declining sales of beer due to reduced market

⁶⁰ Ibid at p6

⁶¹ Ibid at p6-7

⁶² Ibid at p7 and p118

⁶³ Ibid at p7. S and B Webb note that there had been early moves in this direction under the second Beer Act of 1834 and the third Beer Act of 1840, although they ultimately failed to provide any form of effective regulation. Above, n.26 at p129

⁶⁴ Above, n.3 at p27

⁶⁵ Above, n.10 at p6-7

⁶⁶ Above, n.3 at p27

⁶⁷ Ibid at p27

demand.⁶⁸ Further strains were placed on the brewer-publican relationship when the London brewers sought to call in loans and refused the custom of publicans convicted of ‘diluting’, a practice of watering down beer in a bid to increase profit margins.⁶⁹ The situation subsequently prompted publicans to look for new sources of finance, which they found in the Licensed Victuallers Mortgage Association, which was formed in 1887 and lent money to publicans without ties.⁷⁰ Similarly, the Burton Breweries became a source of funding.⁷¹ Therefore, between 1880 and 1900 there were significant changes on the retailing side of the brewing industry.⁷² Prior to this, the country brewers were more heavily dependent on owning retail outlets for their own beer, while the larger Burton and London brewers opted out of direct involvement in retailing to any significant extent.⁷³ They held firm the belief that they were brewers not property owners.⁷⁴ However, after 1880 this position changed drastically with a significant push by brewers for further integration with the result that by 1900 the tied house system prevailed in the retail market.⁷⁵

1.6 Move towards property ownership

Over this period there was a distinctive shift away from the partial loan tie towards brewery ownership of freeholds. This was largely prompted as problems arose due to the size of the loans which spiralled out of control due to rising London property prices.⁷⁶ Issues were also arising due to the incomplete nature of the loan tie as well as the unworkable discounts being offered by Burton and country brewers to the free trade.⁷⁷ Consequently, at the point when loans exceeded one million pounds during the 1880s, brewers’ attention turned to owning the leaseholds and so forging a closer tie with publicans, especially given the ease with which capital could now be raised.⁷⁸ Changes in the laws on limited liability, most notably marked by the Guinness six million pounds issue, enabled brewers after 1884 to take advantage of changes in the law. This was achieved through incorporation which enabled the brewery companies, through share

⁶⁸ Above, n.42 at p89

⁶⁹ Above, n.5 at 69 and above, n.3 at p33

⁷⁰ Above, n.42 at p90

⁷¹ Ibid at p90

⁷² Above, n.3 at p25

⁷³ Ibid at p25

⁷⁴ Ibid at p25

⁷⁵ Ibid at p25

⁷⁶ Above, n.8 at p268-269

⁷⁷ Ibid at p268-269

⁷⁸ Ibid at p269

issues, to raise the capital required to acquire further public houses or to make larger loans on mortgage to secure existing trade.⁷⁹

However, the position differed north and south of the border. Donnachie states that in Scotland, although there is evidence of the larger brewers acquiring public houses, there is little to no evidence of a tied trade in Scotland, much before the middle of the nineteenth century.⁸⁰ Donnachie cites HH Drummond's evidence in 1830 to a parliamentary committee that there had been no complaint of a monopoly in the Scottish brewing trade with few public houses being owned by brewers as confirmation that "*the trade is perfectly free*".⁸¹ The tied house system based on brewery ownership took some time to become established in Scotland. Brewers preferred to develop the retail trade by lending money to publicans to create a partial tie whilst the debt was outstanding.⁸² Consequently, the property tie did not prevail although it was more common.⁸³ The primary reason for the diverging approaches north and south of the border during this period was ultimately licensing.⁸⁴ Similarly to England with the reintroduction of restrictive licensing, retail licences were issued to individuals, not to public houses or other outlets, although in England no restriction was placed on the number of licences one brewer could acquire.⁸⁵ In contrast to the position in England, in Scotland licences could not be traded, with the Scottish magistrates abiding by the principle of 'one man, one licence' and thereby effectively preventing the development of the tied house system based on brewery ownership.⁸⁶ Therefore, as restrictions were placed on the number of licences available, their value and that of the retail outlets, increased significantly.⁸⁷ Whilst this caused brewers in England to compete for tied outlets, due to the differences in licensing in Scotland, Scottish brewers instead opted to extend credit to licensees in return for the exclusive sale of their product.⁸⁸ In addition a practical matter also inhibited the development of the system namely the limited capital available to Scottish brewers by comparison to their English counterparts.⁸⁹ This caused the Scottish brewers to seek out an

⁷⁹ Above, n.5 at 74

⁸⁰ Above, n.13 at p128

⁸¹ Ibid at p128

⁸² Ibid at p181 and p194 citing PP 1899 XXV, Report of the Royal Commission on Liquor Licensing Laws, Final Report, 182

⁸³ In the years 1869-1899. Above, n.13 at p194

⁸⁴ Ibid at p206-207

⁸⁵ Ibid at p206-207 and above, n.3 at p36

⁸⁶ Above, n.3 at p36 and above, n.13 at p206

⁸⁷ Above, n.13 at p206

⁸⁸ Ibid at p206-207

⁸⁹ Above, n.8 at p107

English market and develop their export trade to England and abroad.⁹⁰ Gourvish and Wilson state that some brewers acquired houses in the North East of England, although the loan tie was more heavily relied upon.⁹¹

However, the turn of the century marked the end of the ‘Stock Exchange boom’⁹² during which there had been a significant number of amalgamations. By the early twentieth century the fierce competition amongst brewers to secure licensed premises was over with most public houses now belonging to brewers.⁹³ However, the tied house system was still largely unknown in Scotland in 1914 with the Temperance (Scotland) Act 1913 further discouraging brewers from investing in licensed property by making licences subject to periodic local elections.⁹⁴

1.7 The trend towards greater concentration in the industry

Nevertheless, in the post-First World War era, the trend towards consolidation continued with further amalgamations as companies were cash rich⁹⁵ and acquired other breweries in order to expand their retail base.⁹⁶ Such acquisitions were for the most part linked to the proximity of the tied houses close to the acquiring brewery⁹⁷ as technical advancements also added to the need to ensure that a high level of output was maintained in the larger breweries. Consequently, the chairman of one brewery stated in April 1924 “*what we really want is more trade to enable us to run our brewery (which was a new one) more nearly to its real output capacity. This probably can only be achieved by absorption of some other brewery undertakings, as individual houses are becoming extremely difficult to acquire at a reasonable price.*”⁹⁸

However, throughout the 1920s support for the temperance movement remained strong and at that time the Royal Commission on Licensing was also critical of the tied house system.⁹⁹ Nevertheless, the UK Government did not act on the Committee’s recommendations although the impetus for acquisitions changed significantly after 1920

⁹⁰ Above, n.8 at p107. Gourvish and Wilson state that Scotland’s success was due to the fact that Scottish ales travelled well; the main Scottish brewers were good merchants and took care in shipping their product to Latin America, Australia and India; and they were also pioneers in the bottling of beer. Above, n.8 at p109-110

⁹¹ Above, n.8 at p278

⁹² Above, n.10 at p12

⁹³ Ibid at p17

⁹⁴ Above, n.9 at p34

⁹⁵ Reduced output was off-set by higher prices which resulted in rising profits. Above, n.10 at p24

⁹⁶ Ibid at p26. In the UK the number of brewers licensed to sell beer dropped from 2,464 in 1921 to 1,502 in 1928 to 840 in 1939, with this trend continuing in the twentieth century and beyond. Above, n.8 at p346

⁹⁷ Above, n.10 at p27

⁹⁸ Above, n.10 at p29 quoting Chairman of Meux, April 1924

⁹⁹ Ibid at p33

given the climate of reduced demand.¹⁰⁰ The emphasis was placed strongly on the rationalisation of productive capacity.¹⁰¹

Subsequently, by the end of the 1930s, the industry was even more concentrated.¹⁰² The larger national brewers had strengthened their distribution networks and had sought to take advantage of the increasing popularity of bottled beer.¹⁰³ Bottled beer offered higher margins and lower transport costs. The smaller breweries on the other hand had grown in regional importance chiefly by way of amalgamation and by seeking to tie further outlets to sell their own brands of bottled beer.¹⁰⁴ Consequently, there was a division between national brewers with significant tied estates who also sold branded beer on the national market, and the regional brewers whose markets were more localised and whose trade focused on draught and bottled beer sold through their own tied houses. A number of smaller firms also operated in the UK.¹⁰⁵

However, in Scotland, concentration was slower to occur. The industry was dominated by family owned firms which, prior to 1939, relied heavily on their extensive export trade. This trade was reduced in the post-war era as former colonial customers developed their own brewing industries, forcing the Scottish brewers to compete in the sluggish Scottish market.¹⁰⁶ Brewery acquisitions of public houses therefore increased after 1939 but the majority of public houses remained free of tie. Rationalisation was also slow to occur in Scotland during the 1950s despite the low level of tied trade in the Scottish market.¹⁰⁷ The main obstacle was the reticence of family owners to lose the identity of their own beers and breweries, although some opted to integrate vertically through the acquisition of licensed houses and the loan tie.¹⁰⁸

¹⁰⁰ Above, n.8 at p346

¹⁰¹ Above, n.8 at p346. The general trends and influences in this period were summarised by Sir George Courthope's final speech as Chairman of brewer Inde Coope, prior to its amalgamation with the brewer Allsopp's, as cited at above, n.10 at p36.

"In order to maintain economic production and profitable business it is necessary to maintain the output of our breweries. This has only been possible by an increase in the number of licensed houses which form our distributing agencies. To achieve this, both Allsopp's and ourselves, in common with other large concerns, have acquired from time to time smaller brewing businesses, whose houses have been added to our own. But the supply of small brewing businesses is dwindling, with the inevitable result that competition increases for those that remain. The same causes greatly increase the difficulty in maintaining the free trade, which is of great importance both to Allsopp's and ourselves..."

"The two breweries at Burton are side by side, the different departments...could be consolidated in one set of premises or the other. A single analytical laboratory could serve both breweries..."

¹⁰² There were only 840 breweries licensed to sell beer in the UK in 1939. See above, n.8 at p349

¹⁰³ Above, n.8 at p349

¹⁰⁴ Ibid at p349

¹⁰⁵ Above, n.10 at p55

¹⁰⁶ Above, n.3 at p70

¹⁰⁷ Ibid at p70

¹⁰⁸ Above, n.3 at p70

Nevertheless, in the period 1945-1948, brewers had to operate in a very different climate with allegations of excessive profits circulating in 1948 and a highly restrictive Licensing Bill being proposed.¹⁰⁹ Moreover, threats to the tied house system had been presented by a larger potential free trade in national bottled beer and the rise in popularity of clubs.¹¹⁰ The competitive threat presented by clubs, as well as the emergence of club breweries, had grown out of the dissatisfaction with the increasing prices and beer shortages of the First World War.¹¹¹ Vaizey states that their success and their backward integration into brewing, provides evidence of consumers' turning away from the tied house system.¹¹² However, he acknowledges that their exemption from the most rigid elements of the licensing system made them a significant exception to the tied house system for reasons beyond cheapness.¹¹³

Nevertheless, Vaizey has estimated that by 1950, almost all public houses were tied with approximately 95 per cent of public houses in England and Wales and 80 per cent of those in Scotland being tied to a brewery, at least for beer.¹¹⁴ However, Gourvish and Wilson suggest that these estimates may be a little high and refer to the results of a Brewers' Society Questionnaire as an authoritative statement on the matter.¹¹⁵ This Questionnaire suggests that in 1948, 75 per cent of full on-licences in England and Wales, as compared with only 28 per cent of such licences in Scotland, were owned by brewers.¹¹⁶ Consequently, this demonstrates that brewers in England had come to place significant reliance on the tie as a means of selling their beer, with the practice increasing in importance in Scotland.¹¹⁷

1.8 Oligopolistic equilibrium and increased competition

These traditional retailing methods described above endured. Although the industry itself was to change dramatically in the coming twenty-five years with a tide of mergers, the tied house was to remain the dominant type of on-licensed property.

¹⁰⁹ Above, n.8 at p365

¹¹⁰ Above, n.10 at p36

¹¹¹ Above, n.8 at p413

¹¹² Above, n.10 at p142 and footnote 2, p142

¹¹³ Ibid at footnote 2, p142

¹¹⁴ Ibid at p69

¹¹⁵ Above, n.8 at p408

¹¹⁶ Above, n.8 at p409. An 'on-licence' concerns the licensing of premises where alcohol can be consumed, such as public houses. 'Off-licences' are required for premises that sell alcohol that cannot be consumed on the premises, such as off-licence shops.

¹¹⁷ Above, n.10 at p76

Nevertheless, the concentration of the market had been contracting but it was not significantly concentrated which was largely due to the protected market position enjoyed by most firms.¹¹⁸ Vaizey refers to the oligopolistic situation that existed at the time and ensured 'secure profits' were made.¹¹⁹ He concludes that formal trade agreements were not as important as in other industries, where there were greater threats of market entry.¹²⁰ He consequently notes that national agreements to consciously restrict competition with a view to raising prices or restricting output were not known to exist and local agreements were more concerned with preventing price cuts.¹²¹ Nevertheless, such local co-operation was not complete with firms wishing to increase competition doing so by simply avoiding local meetings and thereafter acting in ignorance of any agreements reached.¹²² However, the lack of national agreements was largely attributable to the fact that trade was protected from outside competition with a natural oligopolistic equilibrium existing.¹²³ This also prohibited any 'wars to the death' as the national brewers were too equal in size for this to be successful.¹²⁴ Moreover, the free market was too tied to allow any significant victories. This state of equilibrium was dependent on the existence of the tied houses system.¹²⁵

However, by the early 1950s the tied house was faced with increased competition from various other sources including national bottled beer brands, the rising popularity of alternative leisure activities, as well as pressure to improve the standard of public houses.¹²⁶ Consequently, brewers began to diversify their commercial interests further than brewing and ownership of public houses with the industry increasingly being regarded as part of the highly competitive leisure market.¹²⁷ However, this need to compete within the leisure market resulted in changes in the competitive strategies within the industry as brewers sought additional resources in order to compete successfully.¹²⁸ Concerns were increasingly raised that the concentration of brewing and public house ownership amongst fewer and fewer undertakings was not in the public interest.¹²⁹ Seldon estimates that brewers owned 85 per cent of on-licensed premises in England and Wales by 1953.¹³⁰ Consequently, scrutiny of the tied house system continued. This was mainly due to its

¹¹⁸ Ibid at p155-156

¹¹⁹ Ibid at p156

¹²⁰ Ibid at p156

¹²¹ Ibid at p157

¹²² Ibid at p157

¹²³ Ibid at p158

¹²⁴ Ibid at p158

¹²⁵ Ibid at p159

¹²⁶ Above, n.8 at p446

¹²⁷ Above, n.3 at p52

¹²⁸ Ibid at p52

¹²⁹ Ibid at p52

¹³⁰ Above, n.9 at 33

monopolistic characteristics that saw brewers enjoy significant profits at the expense of the publican and their customers whilst also restricting the number of brands of beers available to the public.¹³¹

1.9 The growth of the national market and further mergers

Throughout this period the national market in beer continued to develop. Although there had been such a market since the introduction of the railway in the nineteenth century, the tied house system effectively limited this market to a small number of brewery companies whose products already largely enjoyed ‘national status’.¹³² These brewers had successfully surmounted the significant transport costs relative to the selling price associated with delivering to distant markets by focusing on the sale of one or two brands and, thereby, achieving economies of scale.¹³³ Consequently, this elusive market was dominated by a limited number of recognised brands of bottled stout and pale ale, which were retailed by local brewers through their own tied houses.¹³⁴ The situation was intensified by the growth in bottled beer in the inter-war period and beyond which encouraged the companies involved to increase their geographical coverage by acquiring shares in their trading partners equity and reciprocal trading agreements.¹³⁵

This trend developed during the 1960s-1970s and is described by Gourvish and Wilson as a time of “*merger ‘mania’*” in all industries in the United Kingdom.¹³⁶ Most of these mergers were horizontal in nature and resulted in substantial increases in concentration in many industries including brewing.¹³⁷ However, the merger wave in the brewing industry was slightly ahead of this trend. Decisive changes in the industry occurred during the 1950s-1960s.¹³⁸ As a result during the 1960s six major brewery groups emerged, each of which owned a chain of tied houses.¹³⁹

However, Scotland again deviated slightly from this trend. Although in 1960 Scottish Brewers merged with Newcastle Breweries forming Scottish & Newcastle Breweries,

¹³¹ Above, n.10 at p159

¹³² These companies in abbreviated form were Bass, Worthington, Inde Coope, Guinness, Whitbread and Allsopp. Above, n.3 at p53

¹³³ Above, n.9 at p31

¹³⁴ Above, n.3 at p53

¹³⁵ Ibid at p53. The popularity of bottled beer continued throughout the 1950s due to consistency in its flavour and appearance over draught beer whilst the growth in television encouraged home drinking (also ibid at p54)

¹³⁶ Above, n.8 at p447

¹³⁷ Ibid at p447

¹³⁸ Ibid at p448-449 and above, n.3 at p64

¹³⁹ In 1952 the six largest brewers owned 16 per cent of the total number of public houses, increasing to 56 per cent in 1976. Above, n.3 at p57

which continued to expand and develop its market position through further mergers in Scotland, this was a far more expensive process for Scottish brewers than their English counterparts.¹⁴⁰ This level of expense had a limiting effect. Far higher prices had to be paid for public houses in Scotland compared to England. This was due to the fact public houses were sold as independent businesses in their own right, thereby necessitating significant payments for the goodwill.¹⁴¹ Consequently by 1967 less than 30 per cent of Scottish public houses and licensed hotels were owned by brewers.¹⁴²

Nevertheless, as the market continued to contract, Hawkins and Pass estimates that by 1968 the seven largest companies controlled 73 per cent of beer production in the UK.¹⁴³ These companies continued to increase their market share by acquiring smaller companies and by greater infiltration of the free trade.¹⁴⁴ The motivation behind these mergers was the acquisition of retail outlets not productive capacity, and so although horizontal in nature, Gourvish and Wilson remark on this vertical characteristic.¹⁴⁵ Further, in light of the increasing competition for consumers in the leisure market throughout the 1970s,¹⁴⁶ a number of these were conglomerate mergers and subsequently linked brewing with other products and leisure interests.¹⁴⁷ Consequently as this process continued, in comparison to the position in 1955 when the top five breweries owned eleven per cent of Britain's licensed retail outlets, by 1974 they owned 38 per cent.¹⁴⁸ However, there were also rationalisations and synergies in production of beer following on from these mergers which resulted in the closure of over half of the production plants involved.¹⁴⁹ Thus there was a substantial contraction in the industry which resulted in the 'Big Six' breweries, along with Guinness, dominating British brewing for the next thirty years.¹⁵⁰

Various reasons have been suggested for this increase in merger activity, some of which were general economic influences: a buoyant stock market which enabled mergers to take place by way of exchange of shares, not just cash; the continued drive to achieve

¹⁴⁰ Above, n.3 at p70-71

¹⁴¹ Ibid at footnote 41, p71

¹⁴² Ibid at footnote 41, p71

¹⁴³ Ibid at p79

¹⁴⁴ Ibid at p79

¹⁴⁵ Above, n.8 at p450

¹⁴⁶ To maximise returns, public houses had to be seen as places not just for the consumption of alcohol but places of general entertainment. (Above, n.8 at p474.) Four of the largest mergers at this time were Grand Metropolitan Hotels and Truman in 1971, Grand Metropolitan Hotels and Watney Mann in 1972 and Imperial Tobacco Group and Courage in the same year, and Allied and J. Lyons & Co in 1978 (ibid at p450)

¹⁴⁷ Ibid at p450

¹⁴⁸ Ibid at p448-449

¹⁴⁹ Ibid at p449

¹⁵⁰ The six largest breweries were the result of many mergers. They were (in abbreviated form) Allied Breweries, Courage, Bass Charrington, Scottish & Newcastle, Watney and Whitbread along with Guinness. Ibid at p449-450

economies of scale; and the desire to maintain market power.¹⁵¹ However, others were specific to the brewing industry. Hawkins and Pass suggest that the rapid increase in concentration in the industry in 1959-1961 was partly fuelled by the realisation in the City of London that licensed property, being the industry's main asset, was undervalued.¹⁵² This was clearly revealed by the attempted take-over of Cheltenham and Hereford Breweries Ltd in 1955.¹⁵³ This divergence in values and the depressed share value of breweries gained the attention of influential 'entrepreneurs' such as Charles Clore¹⁵⁴ whose unsuccessful bid for Watney Mann in 1959 prompted the brewery to undertake a programme of defensive mergers on a national scale.¹⁵⁵ Further, although the most obvious reason was the continued decline in the demand for beer, which had been the prevailing trend for the previous fifty years, increased demand for bottled beer caused national brewers to seek to expand their retail trade, causing an increase in the absorption of smaller brewers.¹⁵⁶

However, despite the merger mania that had prevailed, it should be noted that a number of smaller regional brewers managed to retain their independence.¹⁵⁷ This was partly due to their rural locations which were not appealing to potential purchasers and to their low level trade.¹⁵⁸ However, Seldon also notes they enjoyed an entrenched position as they had successfully exploited local tastes and benefitted from advantages in distribution costs, whilst also being able to supervise closely their public houses with greater ease than a distant owner.¹⁵⁹ Consequently, by the end of the merger era, the UK brewing industry was largely polarised with huge national brewers and a myriad of smaller regional and local enterprises.

2. Growing concern over the anticompetitive implications of beer tie agreements in the UK market

Notwithstanding the survival of many small groups throughout the merger era, concerns were expressed by both the Government and other public bodies over the conduct of many of the larger brewers, with several critical reports being circulated by the National Board for Prices and Incomes (in 1966 and 1969), the MMC (also in 1969) and the Price

¹⁵¹ Ibid at p450-451

¹⁵² Above, n.3 at p65

¹⁵³ The company's assets were valued at £4.47 million against a book value of £1.6 million, acting as a warning shot to the industry. Above, n.3 at p65

¹⁵⁴ Chairman of Sears Holdings Ltd and a key player in the London property boom in the 1950s

¹⁵⁵ Above, n.3 at p66

¹⁵⁶ Above, n.3 at p63

¹⁵⁷ These included, Matthew Brown, Boddingtons', Marston and Vaux. Above, n.8 at p484

¹⁵⁸ Ibid at p484

¹⁵⁹ Above, n.9 at p31

Commission (in 1977).¹⁶⁰ One of the universal concerns expressed, regarded the practice of brewers passing on post-merger costs to consumers by way of higher prices for beer, wines, spirits and soft drinks.¹⁶¹ However, such behaviour was a largely inevitable consequence of vertical integration as one of the general concerns associated with such a degree of integration is the resulting reduction in competition. This arises from undertakings by-passing one or more levels in the market by engaging not only in manufacturing, but also retailing, and so placing the product directly in the hands of consumers.¹⁶² Consequently, the higher the degree of vertical integration in the brewing industry, the greater the scope for abuse of market power.

2.1 The National Board for Prices and Incomes, the MMC and the Price Commission's concerns over the tied house system

2.1.1 The National Board for Prices and Incomes (1966)

As the brewing industry underwent considerable concentration in the 1960s-1970s, its adjustments were not well received, especially by the National Board for Prices and Incomes (National Board).¹⁶³ Under an arrangement for “*early warning*” of price increases, the Government received notification from several brewers of their intention to increase the wholesale price of certain beers.¹⁶⁴ Before these were approved, the National Board reviewed the structure of costs and prices within the industry, and took into consideration the level of profits already enjoyed.¹⁶⁵ They suggested that the estimated cost increases within the industry had already been largely covered by previous price increases.¹⁶⁶ They found that the tied house system had diminished competition and that the “*brewing industry is too closed an industry to give the consumer the reductions in costs that are associated with innovation.*”¹⁶⁷ They therefore recommended there be no increase in wholesale or retail prices.¹⁶⁸ Further, due to the industry's closed nature as set by the licensing laws, the Government was to consider instituting an enquiry into the control of the sale of alcohol without impeding the entry of new competitors into the industry.¹⁶⁹

¹⁶⁰ Above n.8 at p519

¹⁶¹ Ibid at p519

¹⁶² Above, n.3 at p8

¹⁶³ Above n.8 at p519-520

¹⁶⁴ National Board for Prices and Incomes, *Report No. 13 Costs, Prices & Profits in the Brewing Industry* (Cmnd 2965, 1966) at p iv

¹⁶⁵ Ibid at p iv

¹⁶⁶ Ibid at para 27, p7. Also above, n.8 at p519-520

¹⁶⁷ Above, n.164 at para 44, p12

¹⁶⁸ Ibid at para 47, p12

¹⁶⁹ Ibid at para 56, p14

2.1.2 The MMC (1969)

The foregoing report prompted a reference to the MMC¹⁷⁰ in 1966 regarding the supply of beer for retail sale on licensed premises. They reported in April 1969,¹⁷¹ and focused almost entirely on the level of vertical, rather than horizontal, integration in the industry and found that, amongst others, such level of integration restricted the entry of new products and producers.¹⁷² While numerous factors can conspire to hinder such entry in all markets, including established companies with large market shares and advanced production and distribution facilities, restrictive licensing and the tied house system have long been pin-pointed as the main hindrances in the brewing industry.¹⁷³ The MMC concluded that restrictive licensing reduced competition by imposing limitations on the establishment of new competitors in the licensed trade, and the tied house system operated under these conditions of restrictive licensing had certain negative effects.¹⁷⁴ Included amongst these were the hindered removal of redundant brewing capacity; detriment to the creation by brewers of rational and efficient systems of distribution; the weakening or prevention of the growth of independent wholesalers of wines and spirits; and the hindrance of the entry of new products and producers, thereby weakening competition in the retail trade.¹⁷⁵ Nevertheless, Hawkins and Pass state that the weight afforded to the tied house system in this respect should not be exaggerated as it does not prevent the entry of new products irrespective of consumer demand.¹⁷⁶ This position is supported by the growth of domestic lager production.¹⁷⁷ Lager grew in popularity throughout the 1960s and, initially, almost all lager was imported to satisfy this demand. However by 1976 less than 10 per cent was imported and so the tied house system failed to prevent the entry of a new product.¹⁷⁸ Nevertheless, as Hawkins and Pass also acknowledge, this was largely possible due to the national brewers' extensive distribution systems which ideally placed them to develop such products.¹⁷⁹

The MMC however also noted that competition between brewers was principally to acquire “*captive outlets*” and to improve their amenity, noting that in the on-trade, price

¹⁷⁰ The MMC was then known as the Monopolies Commission

¹⁷¹ National Board for Prices and Incomes, *Report No.136 Beer Prices* (Cmnd 4227, 1969) at para 3, p1. The Monopolies Commission, *Report on the Supply of Beer* (Cmnd 216, 1969)

¹⁷² The Monopolies Commission, *Report on the Supply of Beer* (Cmnd 216, 1969) at para 393, p113

¹⁷³ Above, n.3 at p95

¹⁷⁴ Above, n.172 at para 393, p113

¹⁷⁵ Ibid at para 393, p113

¹⁷⁶ Above, n.3 at p97

¹⁷⁷ Ibid at p97

¹⁷⁸ Ibid at p97

¹⁷⁹ Ibid at p97

competition was almost entirely absent with licensees generally being content to avoid active competition.¹⁸⁰ It observed that:

*“Price competition between tied houses would mean price competition between brewers. The brewers in general would have to stand the adverse effects of retail price competition on the level of their prices and profits, without compensating benefits. We do not think that brewers, especially having regard to their investments in tied houses for the sake of security of market, wish to compete with each other in this way, which would be largely self-defeating from each brewer’s point of view.”*¹⁸¹

Consequently, as noted by Hawkins, the MMC argued that under the tied house system, oligopolistic reticence to engage in price competition had been transmitted from the supply side to the retail trade in the market.¹⁸² It was therefore unsurprising that as brewers owned 48% of all licensed outlets in the UK, including 78% of full on-licensed premises, this was not conducive to the public interest.¹⁸³ The MMC found that the ‘restrictions on competition resulting from the tied house system as operated by brewer suppliers are detrimental to efficiency not only in brewing, but in wholesaling and retailing, and to the interests of independent suppliers and to the interests of consumers.’¹⁸⁴ Hawkins and Pass however remark that the Report was produced at a time when the merger era was just ending and the process of post-merger rationalisation had not gotten under way, and therefore efficiency gains had not yet been realised.¹⁸⁵ Consequently, accurate representation of the established post-merger market may not have been provided. Nevertheless, although the MMC would not recommend the separation of brewing from the ownership or control of retail outlets due to the serious consequential problems that would create, they stated, *“we are of the view that, but for the difficulties of change and transition, a state of affairs in which brewers did not own or control licensed outlets would be preferable to the tied house system.”*¹⁸⁶ Similarly to the National Board it was considered that whilst potentially straying outside the scope of their remit, there were grounds for suggesting that the licensing laws could be amended to assist in addressing the

¹⁸⁰ Above, n.172 at para 393, p113

¹⁸¹ Ibid at para 385, p110-111

¹⁸² Ibid at para 285, p110-111. K Hawkins, ‘The Price Commission and the brewing industry: a critical note’ (1979) 27(3) Journal Ind Econ 287 at 287

¹⁸³ Above, n.172 at para 415, p119 and above, n.3 at p9

¹⁸⁴ Above, n.172 at para 415, p119

¹⁸⁵ Above, n.3 at p80

¹⁸⁶ Above, n.172 at para 401, p115

‘defects’ of the tied house system as currently operated under those laws.¹⁸⁷ While no direct action was taken, it was recommended that the licensing laws be relaxed.¹⁸⁸

2.1.3 The National Board for Prices and Incomes (1969)

Following on from the MMC’s report, in light of the aforementioned arrangement for the early warning of price increases,¹⁸⁹ the industry was once again considered by the National Board in 1969. In reviewing the conditions within the industry, it noted that it faced increased competition from outside itself with, amongst others, restaurants and residential premises obtaining licences to sell alcohol.¹⁹⁰ While competition between on-licensed premises was increasing the National Board shared the MMC’s view that due to the effects of restrictive licensing and the tied house system, “*price competition is at present far from being a fully effective force*”.¹⁹¹ It was however conceded that if competition increased following the MMC’s report discussed above, the industry should be afforded freedom in retail pricing.¹⁹²

2.1.4 Continuing concerns - Price Commission (1977)

Concerns over the tied house system therefore did not dissipate. The Price Commission’s 1977 report contrasted with the foregoing reports which focused on vertical integration, as the degree of horizontal integration was also criticised. It was noted that:

“...the most striking point is the degree of both horizontal, and vertical integration in the industry. Horizontally, the industry is dominated by six concerns who over the years have pursued an aggressive policy of amalgamation and acquisition. Vertically, it is highly integrated from the brewery to the public house...”

Not only is brewing a highly concentrated industry, but there are significant barriers to entry and virtually no competition from imports. These are the classic conditions for a

¹⁸⁷ Ibid at para 410, p117

¹⁸⁸ Above, n.172 at para 416, p119. This proposal was concerned with England and Wales, however, it was noted that brewer ownership of licensed premises in Scotland was increasing and may have a disadvantageous effect. (Ibid at para 414, p119)

¹⁸⁹ This effectively afforded the Government control of wholesale beer prices, and public bar prices. The Board noticed that for over 3 years there had been few increases in the wholesale and public bar prices other than “non quantifiable” quotas or due to duty increases. None of the larger brewers had made “notifiable” price increases since July 1966. National Board for Prices and Incomes, *Report No.136 Beer Prices* (Cmnd. 4227, 1969) at para 5, p1-2

¹⁹⁰ Ibid at para 15, p4

¹⁹¹ Ibid at para 75, p23

¹⁹² Ibid at para 75, p23

monopoly which is likely to operate to the detriment of consumers....the way this trade is organised and run has a profound effect on prices and profits.”¹⁹³

In addition to establishing that the classic conditions for a monopoly existed within the market, the report echoed the concerns surrounding the tied house system raised in previous reports as these largely remained.¹⁹⁴ It concluded that “[t]he combined effect of high concentration and vertical integration has enabled the brewers to exert a high degree of price leadership and to augment the barrier to entering the industry imposed by restrictive licensing laws....The effect of price leadership by managed houses has been to lead prices up. Aggressive price cutting by a publican is almost unknown.”¹⁹⁵

During the 1960s and 1970s, the primary concerns over the UK beer market were therefore the increasingly closed nature of trade and the rapidly diminishing level of price competition largely attributable to the extensive use of the beer tie in conjunction with restrictive licensing. Concerns regarding the industry and the tied house system continued to intensify causing it to be the subject of extensive Government scrutiny which culminated in the 1989 MMC Report.

2.2 The MMC’s 1989 Report and the Beer Orders

In 1989 the MMC published its report ‘The Supply of Beer’¹⁹⁶ (1989 Report) following a reference from the Office of Fair Trading (OFT). Due to the aforementioned concerns over the operation of the market, in 1986 it was reviewed by the OFT. The OFT’s resulting Paper on the possibility of a reference to the MMC highlighted, amongst others, that brewers’ extensive tied estates potentially restricted competition, and that profits, margins and prices were high within the industry.¹⁹⁷ As a result, it recommended that a reference be made to the MMC for them to further investigate the market.¹⁹⁸ The MMC’s 1989 Report

¹⁹³ Price Commission, *Report No.31 Beer Prices and Margins* (1977) at para 6.6, p44-45. Above, n.3 at p79-80

¹⁹⁴ Above, n.3 at p80

¹⁹⁵ Price Commission, *Report No.31 Beer Prices and Margins* (1977) at para 6.5, p44. The inquiry was prompted by the large number of complaints regarding increases in the price of beer. (Ibid at para 1.1 and 1.2, p1)

¹⁹⁶ Above, n.1

¹⁹⁷ Office of Fair Trading, *The Supply of Beer* (OFT 317, 2000) at para 2.1, p2 and J Spicer et al, *Intervention in the Modern UK Brewing Industry* (Hampshire, Palgrave Macmillan, 2012) at p41-42 citing OFT Paper “Possible Monopoly Reference: The Supply of Beer and Tied Houses”, 10 June 1986, paras 27-28. (This was an internal OFT document.)

¹⁹⁸ J Spicer et al, *Intervention in the Modern UK Brewing Industry* (Hampshire, Palgrave Macmillan, 2012) at p48 citing paras 82 and 84, OFT Paper “Possible Monopoly Reference: The Supply of Beer and Tied Houses”, 10 June 1986. (This was an internal OFT document.)

followed and saw it take a far more aggressive approach than that adopted in 1969.¹⁹⁹ Whish describes the Report as “*one of the most remarkable and controversial reports to have been published*”.²⁰⁰

2.2.1 The UK market at the time of review by the MMC

Just prior to the 1989 Report the UK market was only ‘moderately concentrated’ and less so than in most European and North American countries. It consisted of six national breweries,²⁰¹ which together accounted for 75% of UK beer production and 74% of brewer owned retail estate; and fifty-two regional and local brewers that controlled 17% of UK beer production.²⁰² The remainder of the market consisted of brewers who had no tied estate who accounted for approximately 8% of beer production, as well as over 160 micro-breweries operating on a much smaller scale.²⁰³ However, the MMC estimated that approximately 75% of all public houses in Great Britain were owned by brewers and fell into two categories.²⁰⁴ Around 30% were managed public houses in which the publican and the staff were employees of the brewer who set the house’s retail prices and received all the profits.²⁰⁵ The remainder were tenanted and the publicans, who were not employees of the brewer who owned the public house, bought beer from the brewer at the wholesale price and set their own retail prices.²⁰⁶ The publicans paid the brewer rent and earned their living from the retail profit of the public house.²⁰⁷ These tenanted houses tended to be smaller in size than their managed counterparts. However, in both instances the brewer determined what beer could be sold from the premises and from where they had to be bought, which was almost always the brewer himself.²⁰⁸

The MMC also noted that brewers influenced the free-trade via the loan tie to free houses. This allowed brewers to secure exclusivity for their products in the public house owned by the operator or a ‘minimum throughput’ in exchange for a loan at a generous interest

¹⁹⁹ The terms of reference required the MMC to investigate whether a monopoly situation existed in relation to the supply beer for retail sale in the UK. See above, n.1 at para 1.1, p1

²⁰⁰ R Whish, *Competition Law* 3rd Edition (London, Butterworths, 1993) at p576

²⁰¹ In abbreviated form these were Allied, Bass, Courage, Grand Metropolitan, Whitbread and Scottish & Newcastle. See above, n.1 at para 1.11, p2

²⁰² Above, n.1 at para 1.11, p2

²⁰³ Ibid at para 1.11, p2

²⁰⁴ Ibid at para 1.9, p2

²⁰⁵ Ibid at para 1.9, p2 and M.E. Slade, ‘Competition policy towards brewing: Rational response to market power or unwarranted interference in efficient markets?’ in J.F.M. Swinnen, ed, *The Economics of Beer*, (New York, Oxford University Press Inc., 2011) at p183

²⁰⁶ Above, n.1 at para 1.9, p2 and M.E. Slade, ‘Competition policy towards brewing: Rational response to market power or unwarranted interference in efficient Markets?’ J.F.M. Swinnen, ed, *The Economics of Beer* (New York, Oxford University Press Inc., 2011) at p183-184

²⁰⁷ Above, n.1 at para 1.9, p2

²⁰⁸ Ibid at para 1.9, p2

rate.²⁰⁹ Consequently, it was estimated that half of the 25% of public houses not owned by brewers were tied to them by way of loan, as well as half of members' clubs.²¹⁰ It was also estimated that approximately two thirds of all beer sold by brewers, including that for home consumption, was sold through premises they either owned or loan tied.²¹¹ Subsequently, only a very small proportion of the market was entirely free of brewery influence.²¹² It was however acknowledged that the position differed in Scotland. In Scotland there was a far smaller number of premises owned by brewers, although loan tying was far more prevalent.²¹³ The market was also greatly more concentrated with Scottish & Newcastle and Bass sharing 80% of the beer market.²¹⁴ The Report also noted that in Ireland neither the property or loan tie prevailed although Guinness and Bass supplied 90% of the market.²¹⁵

2.2.2 A complex monopoly finding

In light of the foregoing, despite arguments by The Brewer's Society that the market for beer in the UK was highly competitive the 1989 Report concluded that a complex monopoly²¹⁶ existed in favour of brewers with tied estates or loan ties with free houses and restricted competition at all levels.²¹⁷

2.2.3 Exploitation of the monopoly situation contrary to the public interest

The MMC identified numerous practices which it considered amounted to the exploitation of this monopoly situation and were against the public interest.²¹⁸ These included the fact that the price of a pint of beer had risen too quickly in recent years.²¹⁹ This was deemed to

²⁰⁹ Ibid at para 1.10, p2

²¹⁰ Ibid at para 1.10, p2

²¹¹ Ibid at para 1.10, p2

²¹² M.E. Slade, 'Competition policy towards brewing: Rational response to market power or unwarranted interference in efficient markets?' in J.F.M. Swinnen, ed, *The Economics of Beer* (New York, Oxford University Press Inc., 2011) at p185

²¹³ Above, n.1 at para 1.13, p3

²¹⁴ Ibid at para 1.13, p3

²¹⁵ Ibid at para 1.13, p3

²¹⁶ "*Complex monopoly situation*" was defined in s.11 Fair Trading Act 1973. Such a situation existed when two or more unconnected entities, together supplying 25% or more of a specified market, acted so as to prevent, restrict or distort competition in connection with the production or supply of goods or services in that market. Above, n.198 at p55

²¹⁷ Above, n.1 at para 1.18-1.19, p4

²¹⁸ Due to the detail of the review of the market conducted by the MMC it is not possible to cover here all of the issues addressed in its 1989 Report. The focus will be on the main issues concerning the operation of the beer tie. Issues including amusement machines with prizes, soft drinks, spirits, rent determinations, licensing laws and restrictive covenants will not be considered

²¹⁹ Since 1976 the price of a pint of bitter in managed houses had increased by 15% in real terms and so was over the rate of general inflation. There was a similar increase in the wholesale price of draught beer between 1980-1986. Above, n.1 at para 12.3-12.4, p266

be the result of the complex monopoly.²²⁰ As so many pubs were tied to the owning brewer, thereby closing them to competing suppliers, wholesale competition was “*severely limited*”.²²¹ The MMC found that even with regard to free public houses and clubs, brewers opted to compete through subsidised loans with their associated exclusive purchasing obligations, rather than through prices.²²² Due to this lack of competition in the market and as brewers’ charged their tenants wholesale prices that were sufficiently high to cover any rent subsidies given to tenants, wholesale prices were higher than they would have been in a competitive market.²²³ These high wholesale prices ultimately resulted in tenants and free houses charging higher retail prices.²²⁴ This was so regardless of whether the house enjoyed a local monopoly or was surrounded by competitors.²²⁵ As a result the MMC found that tenants and free houses failed to offer effective competition to the brewers’ managed houses at the retail level.²²⁶ The retail prices charged in managed houses were therefore maintained at a higher level than would have been permissible in a competitive market.²²⁷

The MMC also found that the retail price of lager was substantially higher than ale even although some brewers could produce it at a similar or lower price than some of their ales.²²⁸ These higher prices were deemed to exemplify the brewers’ ability to set and maintain prices in the wholesale and retail markets.²²⁹ The higher price of lager was therefore due to brewers’ pricing practices rather than the cost of production.²³⁰ The MMC also identified regional price differences for beer in on-licensed premises. While it was acknowledged that retail price differences could be influenced by variations in operating costs, the MMC had evidence of differences in wholesale prices which were not influenced by property and retailing costs.²³¹ These were considered to be the result of the brewers’ policy to set different wholesale prices in different regions.²³² It was noted that the regional price differential in off-licence prices was significantly less than in the on-trade even although they were considered to face similar trends to brewers in retailing costs.²³³ In the off-trade, however, purchasers had competitive power and had access to alternative sources

²²⁰ Above, n.1 at para 12.7, p267

²²¹ Ibid at para 12.7, p267

²²² Ibid at para 12.7, p267

²²³ Ibid at para 12.7, p267

²²⁴ Ibid at para 12.8, p267

²²⁵ Ibid at para 12.8, p267

²²⁶ Ibid at para 12.8, p267

²²⁷ Ibid at para 12.8, p267

²²⁸ Ibid at para 12.9, p267

²²⁹ Ibid at para 12.14, p268

²³⁰ Ibid at para 12.16, p268

²³¹ Ibid at para 12.18, p269

²³² Ibid at para 12.18, p269

²³³ Ibid at para 12.20, p269

of supply including brewers in continental Europe.²³⁴ In the on-trade, brewers' pricing strategies had inhibited the growth of an independent wholesaling sector, which by posing competition on a significant scale could have challenged whether these differences were justified.²³⁵ Consequently the regional price differences were attributed to the existence of the monopoly situation.

Tied and managed houses were also noted to lack the ability to freely choose what drinks they stocked in order to meet consumer demands.²³⁶ Free houses and clubs who had accepted a loan tie were similarly restricted.²³⁷ Therefore consumers in some pubs may not have been able to buy the product of their choice, but would be offered an alternative of 'similar character'.²³⁸ Nevertheless, as consumers considered there were differences between brands, consumer choice was affected by the tied house system.²³⁹ While it was acknowledged that it was not practical for pubs to stock all brands of all drinks, brewers decided what products were supplied, not consumers.²⁴⁰ Tying agreements were therefore found to restrict the ability of the pub's proprietor to respond fully to consumer demands, with this being particularly serious where there was a concentration of pubs owned by an individual or small group of companies in a particular area.²⁴¹

The MMC also addressed the position of tenants of public houses. They highlighted their lack of security of tenure and the lack of a legally binding Code of Practice for brewers. Brewers were therefore considered to be able to significantly restrict the independence of their tenants and thereby strengthen their own ability to exploit and maintain their monopoly.²⁴²

The MMC turned to consider the impact of the complex monopoly on the position of wholesalers in the market. In doing so it noted that the role of the independent wholesaler was to facilitate supplies to smaller retailers whose requirements were not sufficient to

²³⁴ Above, n.1 at para 12.20, p269

²³⁵ Ibid at para 12.21, p269

²³⁶ Ibid at para 12.53, p275

²³⁷ Ibid at para 12.56, p275

²³⁸ Ibid at para 12.57, p276

²³⁹ Ibid at para 12.58, p276

²⁴⁰ Ibid at para 12.58, p276

²⁴¹ Ibid at para 12.58-12.59, p276. Local concentration of brewer-owned public houses was addressed by the MMC. It was noted that in some rural and urban areas consumer choice of public house was limited with pubs offering the same range of drinks when owned by the same brewer (ibid at para 12.29, p271). It was not considered satisfactory that a consumer should be forced to rely on the use of their car to avoid a concentration of a particular brewer's pubs (ibid at para 12.31, p271). While it was accepted that public houses compete more on the basis of amenity than on price or range of products, when brewers own a large proportion of public houses in a particular area, the opportunity for different forms of competition to come into effect was considered to be limited (ibid at para 12.33, 271).

²⁴² Ibid at para 12.48, p274

justify direct deliveries from manufacturers.²⁴³ They were considered central in enabling smaller brewers to achieve national distribution.²⁴⁴ Despite the increasing range of drinks offered in the UK market wholesalers' activities were found to be very limited and so provided little competition to the brewers' wholesaling operations.²⁴⁵ The MMC attributed this lack of competition to brewer policies²⁴⁶ and noted that their hostility was largely influenced by their fear that the development of such competition would threaten their own wholesaling and retailing activities.²⁴⁷ The MMC's expectation was that in 'proper' market conditions, independent wholesalers would offer customers, on cost effective terms, a range of brewers beers and products thereby presenting licensees with a genuine choice as they could opt to accept brewers products from a brewer owned wholesaler or an independent wholesaler.²⁴⁸

Brewer reliance on the loan tie to secure trade was also found to reduce the opportunity for other brewers to compete for business as well as restricting consumer choice.²⁴⁹ It was therefore also found to restrict or distort the entry of new suppliers and to inhibit smaller brewers from increasing their free-trade sales against the public interest.²⁵⁰

These numerous concerns subsequently prompted a legislative strike on the traditional tied house structure in the UK which had far reaching implications for the Big Six national brewers and the industry generally.²⁵¹ Some of these were potentially unforeseen and are still affecting the industry today.

2.3 The Beer Orders

Due to the findings of the 1989 Report and its recommendation that measures be taken with a view to "*increase competition in brewing, wholesaling and retailing, encourage new entry, reduce prices and widen consumer choice*",²⁵² the Secretary of State subsequently made two Orders. These were the Supply of Beer (Tied Estate) Order 1989²⁵³ and the Supply of Beer (Loan Ties, Licensed Premises and Wholesale Prices)

²⁴³ Ibid at para 12.82, p280

²⁴⁴ Ibid at para 12.82, p280

²⁴⁵ Ibid at para 12.82, p280

²⁴⁶ The MMC established that brewers often restricted the range of products made available to wholesalers and made it a condition of supply that wholesalers would not trade with the brewer's tenants or those loan tied to them. Ibid at para 12.85, p280

²⁴⁷ Ibid at para 12.87, p281

²⁴⁸ Ibid at para 12.89, p281

²⁴⁹ Ibid at para 12.77, p279

²⁵⁰ Ibid at para 12.77, p279

²⁵¹ J Manley (ed), 'Market Report 2007 Breweries & The Beer Market' (Key Note) at p26

²⁵² Above, n.1 at para 1.32, p5

²⁵³ SI 1989/2390, hereafter referred to as the Tied Estate Order

Order 1989,²⁵⁴ together known as the ‘Beer Orders’. However, due to intensive lobbying following the publication of the MMC’s Report, these were a diluted version of the original recommendations proposed.²⁵⁵ Nevertheless, the Orders were intended to loosen the tie between brewing and pub retailing, thereby easing market entry and encouraging competition.²⁵⁶ They ultimately severed the tie between brewing and retailing for the largest brewers and greatly shook the industry. The most controversial requirement, which departed from the MMC’s position in 1969 when it actively chose not to divest brewers of their public houses due to the potential implications, was detailed in The Tied Estate Order. This constituted an extreme intervention in the market. It targeted those brewers and ‘large brewery groups’ with interests in excess of two thousand ‘licensed premises’ and capped the number of ‘licensed premises’²⁵⁷ that could be owned by such vertically integrated brewers.²⁵⁸ These were effectively only the Big Six at that time. It was therefore key in the restructuring of the industry. Brewers were required to have reduced their tied estates to no more than 2,000 licensed premises or to have released the ties on half of the premises above that number by November 1992.²⁵⁹ They therefore essentially had to decide whether to cease brewing and focus on retailing or whether they should retain their brewing interests and sell or lease their pubs free of tie.²⁶⁰ Moreover, brewers with more than 2,000 tied premises had to allow them to serve at least one cask-conditioned ale²⁶¹ from a supplier other than the landlord, known as a Guest Beer.²⁶² The brewers were also prohibited from tying non-alcoholic beer or other drinks.²⁶³ The primary aim of this Guest Beer Provision (GBP) was to afford greater choice to the tenants who wanted to offer a

²⁵⁴ SI 1989/2258, hereafter referred to as the Loan Tie Order

²⁵⁵ M.E. Slade, ‘Beer and the Tie: Did divestiture of Brewer Owned Public Houses Lead to Higher Beer Prices?’ (1988) 108 *The Economic Journal* 565 at 571. The original recommendation of the MMC was the imposition of a ceiling of 2,000 on the number of on-licenses any brewer could own, thereby necessitating the divestiture of 22,000 premises by the national brewers. (Above, n.1 at para 12.129, p288.) All loan ties were to be eliminated with current loans being allowed to run their course. (Above, n.1 at para 12.152, p293) Tenants were to be allowed to purchase a minimum of one brand of draught beer from a supplier other than their landlord (n.1, at para 12.137(a), p290). Tenants were also to be brought within the provisions of the Landlord and Tenant Act 1954 (n.1, at para 12.141, p291). Brewers were to publish wholesale price lists (ibid at para 12.158, p294). Also above, n.212 at p185.

²⁵⁶ Office of Fair Trading, *The Supply of Beer* (OFT 317, 2000) at para 2.2, p2

²⁵⁷ This was widely defined by Article 1(2) of the Tied Estate Order to cover all on-licensed premises and clubs in England and Wales. In Scotland it covered premises with a public house licence, a hotel licence or a refreshment licence.

²⁵⁸ Article 2, Tied Estate Order

²⁵⁹ Article 2, Tied Estate Order

²⁶⁰ V Edwards and L Bunting, ‘Licensed Premises: Part 1 the Changing Strategies of National Brewers’, (1992) 10(4) *Property Management* 319 at p325

²⁶¹ ‘Cask-conditioned beer’ is defined in Article 7(3) of the Tied Estate Order as “*beer which undergoes fermentation in the container from which it is served for consumption*”.

²⁶² Article 7, Tied Estate Order

²⁶³ Ibid

wider range of products to their customers.²⁶⁴ Further, the Loan Tie Order effectively required that brewers supply the wholesale trade unless they had a sound commercial reason for refusing to do so.²⁶⁵ They also required the introduction of a three-month notice period on termination of which the borrower should be released from any loan held with the brewer.²⁶⁶ The use of restrictive covenants when selling premises was prohibited and the brewer was required to publish the list prices for the wholesale supply of beer.²⁶⁷

Consequently, although the Beer Orders were weaker than the MMC's recommendations they were very prescriptive and constituted an extreme intervention in the market. They were also stricter in their terms than the EU competition rules in force at that time.²⁶⁸

2.3.1 Impact of the Beer Orders on the UK beer market

The Beer Orders caused a substantial shake-up within the brewing industry and saw changes occur throughout the 1990s that have shaped it today. Each of the Big Six operated up to 7,000 public houses at the time of the Orders and were therefore required to divest most of their tied estates. Brewer ownership of on-licenses subsequently declined by 14,000, which exceeded the 11,000 required by the Beer Orders.²⁶⁹ Managed houses tended to be larger, and so more profitable, and therefore most of the pubs that were sold were tenanted.²⁷⁰ Of the tenanted pubs remaining, the majority were converted from three year to long leases, thereby making the tenant of these leased houses responsible for a

²⁶⁴ The European Commission investigated the GBP following a complaint from a British-based importer of German beer which claimed it was excluded from the UK's guest beer market. The Commission threatened a legal challenge to the UK on the basis that the application of these provisions amounted to unfair discrimination against imports. (C.C. Milne and P Spink, 'Calling time on the guest beer provision' (1997) 18(2) E.C.L.Rev 79 at 79 and The European Ombudsman, *Annual Report 1998* [1999] OJ C300/1 at 61-62). Cask-conditioning predominated in the British Isles and so the provisions were potentially discriminatory against other European brewers. (C.C. Milne and P Spink, 'Calling time on the guest beer provision' (1997) 18(2) E.C.L.Rev 79 at 79-80) The EU however recognised that the GBP had the objective of increasing consumer choice and creating market opportunities for traditional beers produced by small and medium sized brewers. (The European Ombudsman, *Annual Report 1998* [1999] OJ C300/1 at p62). Following consultation with the European Commission and the European Parliament (House of Commons Second Standing Committee on Delegated Legislation, Draft Supply of Beer (Tied Estate) (Amendment) Order 1997, (15th July 1997) and The European Ombudsman, *Annual Report 1998* OJ [1999] C300/1 at para (iv), p62-63) the Supply of Beer (Tied Estate) (Amendment) Order 1997 SI 1997/1740 came into force. This permitted tied tenants to buy one brand of bottle-conditioned beer, which included most traditional beers produced in the EU, in addition to the cask-conditioned beer. (Article 2, The Supply of Beer (Tied Estate) (Amendment) Order 1997 SI 1997/1740 and The European Ombudsman, *Annual Report 1998* OJ [1999] C300/1 at para (v), p63)

²⁶⁵ Article 5, Loan Tie Order

²⁶⁶ Article 2, Loan Tie Order

²⁶⁷ Article 3 and Article 4, Loan Tie Order

²⁶⁸ Commission Regulation (EEC) 1984/83 of 22 June 1983 on the application of Article 85(3) of the Treaty to categories of exclusive purchasing agreements ((1983) OJ L173/5). This is discussed in Chapter 3. The EU Commission found that UK law was not incompatible with the supremacy of EU law on the basis that it did not strike at the root of the Block Exemption. Above, n.200 at p577

²⁶⁹ Above, n.212 at p186

²⁷⁰ Ibid at p186

greater proportion of capital improvements to them.²⁷¹ However, contrary to the intentions of the MMC, independent purchasers were slow to enter the market due to the recession and the subsequent property slump in the period following the Beer Orders.²⁷² Furthermore, a complex series of events subsequently took place within the industry. These included several mergers and some companies engaging in a “*pub for breweries swap*”,²⁷³ which ultimately caused even greater consolidation which was indeed contrary to the aims of the MMC Report. Consequently, by the compliance date in 1992, the brewing industry was as concentrated as it had ever been, and there was now an even tighter and more complex oligopoly in existence. The largest brewers enjoyed 60 per cent of beer sales in March 1992, compared to only 46 per cent of beer sales in 1989.²⁷⁴ This was accompanied by a corresponding increase in beer prices which exceeded inflation over the same period, thereby having the opposite effect from that intended by the reforms.²⁷⁵

Further, as part of the major changes that continued to occur throughout the 1990s, the Big Six took actions which resulted in all but one of them exiting brewing by the year 2000.²⁷⁶ In 1991 Grand Metropolitan was the first to leave brewing, selling its breweries to Foster’s Brewing Group, the Australian based owner of Courage and another of the Big Six.²⁷⁷ In 1993 Allied Breweries merged with the UK brewery owned by Carlsberg to form Carlsberg Tetley. This was a joint venture company that eventually withdrew from brewing and instead focused on wines and spirits when Carlsberg took full control of the joint venture in 1997.²⁷⁸ Bass was the largest of the Big Six brewers at the time the Beer Orders were adopted. They opted to stay in brewing but in 2000 Bass Brewers was eventually sold to Interbrew, as was Whitbread’s brewing division in the same year.²⁷⁹ Furthermore, Scottish & Newcastle which was the smallest of the Big Six at the time the

²⁷¹ Leased houses were operated in much the same way as tenanted houses. They were owned by the brewer but operated by the lessee who purchased beer from that brewer and set the retail prices charged. Ibid at p186 and R Hucker, (ed), ‘Market Report 2013, Public Houses’ (Key Note, 2013) at p5

²⁷² Above, n.200 at p479-480

²⁷³ Such an agreement was announced in March 1990 shortly after the Beer Orders. Grand Met transferred its brewing business to Courage whilst both companies’ public houses, with the exception of Grand Met’s managed public houses, were transferred to a joint venture company owned equally by them. This company was called Innpreneur Estates Limited. Under the terms of the agreement, these public houses were to be tied to ten-year beer supply agreements with Courage. Given that Grand Met was now free of its brewing interests it was no longer bound by the terms of the Beer Orders, unlike Courage. However, while the deal was permitted despite the fact that it reduced the number of national brewers in operation, thereby increasing concentration, following negotiations with the MMC the length of the beer supply contracts had to be reduced. As a result Courage was allowed a seven-year supply contract with Innpreneur’s public houses and a four-year contract with Grand Met’s managed pub divisions. Above, n.198 at p130 and p140

²⁷⁴ Above, n.200 at p480

²⁷⁵ Ibid at p480

²⁷⁶ D Fenn, (ed), ‘Breweries & the Beer Market 2002 Market Report’ (Key Note) at p19

²⁷⁷ Ibid at p18

²⁷⁸ Ibid at p18

²⁷⁹ Ibid at p18-19

Beer Orders were implemented grew to be the UK's largest brewer on acquiring Courage from Fosters in 1995.²⁸⁰ They also became involved in the international brewing industry when in 2000 they acquired Kronenbourg, the largest French brewer.²⁸¹

Thus, by 2000 all but one of the Big Six had left brewing and so another consequence of the Beer Orders was that they created the perfect opportunity for powerful foreign multinationals to enter and to dominate the UK beer market. This was exemplified by Grand Metropolitan's sale of its brewing division to the Australian company, Foster's Brewing Group; the acquisition of Bass and Whitbread's brewing divisions by Interbrew, a multinational brewer based in Belgium which was forced in 2001 to sell the Bass brands to Adolph Coors of the US as a result of a Competition Commission Inquiry;²⁸² and the acquisition of Allied Breweries by the Danish company Carlsberg, with the result that by 2001, half of British brewing was in foreign hands.²⁸³ By contrast to the national brewers, the sole focus of these foreign companies is brewing, but on an international scale.²⁸⁴ They place upmost importance on the maintenance of a powerful portfolio of brands as a means of securing a loyal customer base and providing protection against price competition.²⁸⁵ Nevertheless, a strong regional brewing base was also maintained thereby preserving the polarised nature of the UK beer market.

Even although all but one of the Big Six had disposed of their brewing interests during the 1990s, the majority remained committed to their pub divisions throughout this period. However, by the end of the decade, a new breed of company with no formal associations with any breweries emerged which came to be known as pubcos and owned the largest pub estates.²⁸⁶ These developed as brewers divested their pubs in accordance with the terms of the Beer Orders. Whilst some were bought by individuals, thereby creating free houses as anticipated, large blocks of public houses were bought by non-brewing companies, many of which already had interests in the hotel, food and entertainment businesses.²⁸⁷ These companies, which focus purely on retailing operations, subsequently entered into long-term purchasing agreements with the largest brewers for the supply of beer to their newly

²⁸⁰ Ibid at p19

²⁸¹ Ibid at p19

²⁸² Competition Commission, *Interbrew SA and Bass plc: a report on the acquisition by Interbrew SA of the brewing interests of Bass plc* (Cm 5014, 2001) at para 1.18

<http://webarchive.nationalarchives.gov.uk/20111202195250/http://competition-commission.org.uk/rep_pub/reports/2001/452interb.htm - full> accessed 13th April 2015. Above, n.276 at p1. For further discussion on Interbrew, now Anheuser Bush InBev, see Chapter 5.

²⁸³ Above, n.276 at p1 and p18

²⁸⁴ Above, n.251 at p27

²⁸⁵ D Vrontis, 'Strategic assessment: the importance of branding in the European Beer Market' (1998) 100/2 *British Food Journal* 76 at 78 and 82

²⁸⁶ Above, n.276 at p19

²⁸⁷ Above, n.212 at p186

acquired tied estates. Many of these agreements with brewers imposed exclusive dealing clauses on the pubcos.²⁸⁸ Consequently, although the Beer Orders removed the rental payments the national brewers received from many of their tied houses, the beer tie essentially remained.²⁸⁹

One of the first pubcos was created in the early 1990s when, following the sale of their breweries, Grand Metropolitan and Courage placed their tenanted and leased pub estates in a joint venture named Innpreneur and formed the UK's largest grouping of public houses.²⁹⁰ By 2001 Innpreneur had a tied estate of 5,500 pubs which were subsequently sold to other pubcos in 2002.²⁹¹ Furthermore, having retained their pub estate for most of the 1990s, Allied Domecq sold their estate to Punch Taverns, another new pubco.²⁹² In the meantime Bass and Whitbread having already disposed of, or significantly reduced their brewing capacity, also opted to sell their tied estates to Enterprise Inns, another pubco.²⁹³ Thus, only Scottish & Newcastle was left with an interest in both brewing and public house ownership. However the conclusion of this ten year process of dismantling the traditional 'vertically integrated brewer-landlord business model' favoured by the national brewers came with Scottish & Newcastle's decision to sell its retailing division in May 2003.²⁹⁴

Prior to Scottish & Newcastle's disposal, the Beer Orders resulted in the Big Six disposing of more than 14,000 public houses. This exceeded the 11,000 that had been estimated, with the vast majority of them falling into the hands of various pub companies. This was a development that was unforeseen by the MMC when it reported in 1989.

2.3.2 The emergence of the pubco

The pubco essentially performs traditional pub-related activities. These include ownership and maintenance of public houses and the supply of beer. These were once the exclusive preserve of brewers who had required large tied estates in order to achieve the economies of scale that made the tie work efficiently.²⁹⁵ In fact, the pubcos have perpetuated the tied house system by owning estates to rival those of the Big Six whilst also sourcing supplies from a single brewer. The single brewer is often the largest brewer with the strongest

²⁸⁸ Ibid at p186

²⁸⁹ Ibid at p186

²⁹⁰ Above, n.276 at p19

²⁹¹ Ibid at p19

²⁹² K Hughes, (ed), 'Market Report Plus 2009 Public Houses' (Key Note) at p36

²⁹³ Above, n.276 at p19

²⁹⁴ M Dunn, (ed), 'Market Report 2003 Breweries & the Beer Market' (Key Note) at p52.

²⁹⁵ D Fenn, (ed), 'Market Report Plus 2010 Public Houses' (Key Note) at p15

brands that is also able to offer the largest discounts.²⁹⁶ Consequently this arrangement prevents each outlet acting as a free house that sources its own supplies.²⁹⁷ Whilst some pubco owned public houses are directly managed by the pubcos themselves, where the public house is tenanted the relationship between the pubco and its tenant is committed to a lease.²⁹⁸ Pubcos generally secure their income from public houses via three separate revenue streams. Firstly, they benefit from the wholesale profit also referred to as the ‘wet’ rent, which is essentially the price differential between the price paid to suppliers for tied products and the wholesale price at which it is sold to their tenants.²⁹⁹ Secondly, they collect the property or ‘dry’ rent which is subject to review at regular intervals.³⁰⁰ Thirdly, they derive income from any amusement machines within the public house.³⁰¹ Essentially, the combination of these three revenue streams, together with any benefits afforded by the pubco to the tenant, are meant to equal the ‘rent’ that would be paid by a free from tie tenant.³⁰² However, regardless of the style of lease relied upon the central condition is that the tenants, who were previously tied to a national brewer, are now required to source their supplies from the pubco. The pubco determines the prices charged (this is not left to the open market) and flow-monitoring equipment is used to ensure tenants do not purchase beer outside of the tie.³⁰³ Additionally, and in contrast to the position of brewers following the Beer Orders, pubcos are able to tie tenants in respect of non-beer products such as spirits and cider.³⁰⁴

As already mentioned above, Innpreneur was one of the first pubcos to emerge and subsequently provided the business model for pubcos over the next ten years.³⁰⁵ As it was essentially a property-holding company it had to demand the highest rents possible from its lessees. This caused rents to be far higher than they were under previous tenancies and forced lessees to raise the price of beer sold on their premises in order to cover their costs.³⁰⁶ Many pubco chains evolved during the 1990s and early 2000s with Punch Taverns and Enterprise Inns acquiring 16,000 pubs, which had largely been released from the

²⁹⁶ C Lewis, ‘The Future of British Brewing: Strategies for survival’ (2001) 10 *Strategic Change* 151 at 156

²⁹⁷ I Gower, (ed), ‘Market Report Plus 2005 Public houses’ (Key Note) at p4

²⁹⁸ Two different models of tenancy agreements are used. As already mentioned, tenancy agreements were widely relied on by national brewers and are preferred by regional brewers today. Long leases were developed by the pubco Innpreneur and are now widely used by pubcos. Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at para 83, p28

²⁹⁹ Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at para 81, p27

³⁰⁰ *Ibid* at para 81, p28

³⁰¹ *Ibid* at para 81, p28

³⁰² *Ibid* at para 81, p28

³⁰³ *Ibid* at para 94-95, p31

³⁰⁴ *Ibid* at para 94, p31

³⁰⁵ Above, n.292 at p24

³⁰⁶ Above, n.296 at 156

estates of the Big Six.³⁰⁷ Pubcos effectively removed the brewers and the publicans from property ownership. However, due to the need to achieve economies of scale similarly to the brewers before them, consolidation in the pubco market was inevitable. Punch Taverns and Enterprise Inns were the two main players, with estates large enough to rival the size of those of the Big Six.³⁰⁸

2.4 Revocation of the Beer Orders

The rise of the pubco subsequently resulted in the Beer Orders replacing one group of powerful players with another. The OFT's 2000 Report 'The Supply of Beer'³⁰⁹ (2000 Report) considered whether the Beer Orders were still required under the new market conditions. The relevant markets affected by the Beer Orders were defined by the OFT in order to establish a framework for the analysis of what the future of the Beer Orders should be. At the brewing level this was the market for the supply of all beers in the UK. At the retail level the on and off trade were deemed to be in separate markets.³¹⁰

2.4.1 Observations about the UK beer market

In the course of its review, the OFT made several observations about the UK beer market. It was noted that since 1989 over one third of the UK's pubs had been transferred into the

³⁰⁷ Above, n.251 at p27

³⁰⁸ By 2004 they owned over 8,000 public houses each and so controlled almost 30% of all public houses. Above, n.299 at para 17, p11. The MMC noted in its 1989 Report that in 1985 the National Brewers, with the exception of one, owned more than 5,000 on licensed properties. Above, n.1 at para 2.107, p39

³⁰⁹ Above, n.256

³¹⁰ Above, n.256 at para 2.9, p3. The MMC's 1989 Report did not include specific analysis of market definitions, prompting the OFT to undertake this task (ibid at para E.1, p25). The OFT stated that the competition issues addressed in the 1989 Report and the Beer Orders did not require that the product market was narrowly defined. The Beer Orders were focused on the beer tie between brewers and their pub estates and covered all types of beer available in pubs. Importance was therefore placed on the specific way in which beer was retailed in the UK as well as the control brewers exercised over the retail market. As such, focus was placed on the overall reduction in the retail choice of beer not the effects of the beer tie in individual product markets, such as lager (ibid at para E.11, p26-27). The MMC considered there to be significant structural differences between the on and off trade (above, n.1 at para 2.87-2.88, p35) This was followed by the OFT (above, n.256 at para E.13, p27) The OFT however suggested that grounds now existed for widening the definition of 'public houses' implicit in the 1989 Report (ibid at para E.17, p28) due to the changing nature of the pub, with many now placing an emphasis on the provision of food, which the OFT dubiously stated made them virtually "*indistinguishable from restaurants*" and due to the increasing variety of on-trade establishments for the consumption of beer such as clubs and even the bar facilities at leisure outlets (ibid at para E.17-18, p28). As pubs now competed with a wider retail market than before the Beer Orders, the OFT deemed it appropriate for the purposes of their review for all fully on-licensed premises to be used as the framework for assessing competition at the retail level (ibid at para E.19, p28). This would rightly be criticised in later reports on the market. (See Chapter 4) The geographical market was similarly broadly drawn. While stating that it was likely that local markets exist for the on-licensed retail trade, there was no satisfactory basis for determining the boundaries of those markets (Above, n.256 at para E.20, p28). Following the Beer Orders, it was stated that competition conditions were increasingly similar across local markets and so "*even although the retail market is unlikely to be national*" it was deemed that the conditions of competition at this level provided an adequate proxy for those at the local and regional level (ibid at para E.20, p28). Consequently aspects of the market were widely drawn for the OFT's review.

ownership of retail pub chains which had subsequently developed a degree of countervailing buyer power in relation to the national brewers.³¹¹ Furthermore, the declining demand for beer and the new countervailing buyer power presented by pub companies caused further consolidation in UK brewing.³¹² It was considered that only two or possibly three national brewers were likely to remain in the UK market.³¹³ The 2000 Report also noted that with the exception of microbrewers, entry into the UK brewing market was limited with substantial barriers to entry and expansion remaining.³¹⁴ Economies of scale had an even more significant role in production, and expenditure on lager brands and more recently ale brands had increased thereby contributing to those barriers.³¹⁵ These factors favoured the national brewers and limited entry into the UK brewing market, which again was contrary to the aims of the MMC.³¹⁶

Small brewers also still faced difficulties in accessing wholesale and distribution markets in the on-trade due to the substantial discounts offered by national brewers to the pubcos.³¹⁷ The 2000 Report noted that small brewers and independent wholesalers could not match these levels of discounts as they lacked the necessary economies of scale in production as well as the economies of scope in distribution.³¹⁸ Tied loans also had the potential to foreclose the wholesale on-trade market to them.³¹⁹ The 1989 Report had stated that the ultimate test for the Beer Orders was whether an independent wholesale and distribution sector had emerged. This was due to its importance in reducing the barriers to entry faced by smaller and new brewers thereby increasing competition on the market overall.³²⁰ Clearly such an independent wholesale and distribution sector had not developed, with the vast majority of beer sold to the on-trade being distributed by the national brewers.³²¹ Nevertheless, in examining the concerns raised by the MMC in 1989, the OFT concluded that, subject to the retention of certain provisions, the Beer Orders were no longer required.

³¹¹ Above, n.256 at para 2.7, p3

³¹² Ibid at para 2.10-2.11, p4

³¹³ Ibid at para 2.11, p4

³¹⁴ Ibid at para 2.12, p4

³¹⁵ Ibid at para 2.12, p4

³¹⁶ Ibid at para 2.12, p4

³¹⁷ Ibid at para 2.13, p4

³¹⁸ Ibid at para 2.13, p4

³¹⁹ Ibid at para 2.13, p4

³²⁰ Numerous references were made throughout the MMC's 1989 Report to the importance of competition at this level with many of the MMC's recommendations intending to improve this. See for example, above, n.1 at para 12.89-12.90, p281

³²¹ Above, n.256 at para 2.14, p4

2.4.2 Pricing issues no longer a concern in the UK beer market

One of the MMC's major concerns had been real increases in beer prices. The OFT noted that with the new increased buyer power at the retail level, the pubco had brought about a reduction in the average net wholesale price of beer, although this had failed to filter through to the average retail price of beer in the on-trade.³²² This was not however considered to indicate a failure in competition at the retail level.³²³ This was excused on the basis that retail competition was manifest in the greater level of amenity offered by pubs, with consumers also benefitting from greater choice of amenity and price combinations with the emergence of the lower-priced pubco outlets.³²⁴ The distinction between pubs and other on-trade outlets was considered to have been clouded with the OFT establishing that pubs were increasingly competing with clubs, bars, and to some extent restaurants.³²⁵ On-going changes in the licensing regime were deemed to be easing the entry process at the retail level.³²⁶ Although on-trade beer prices had risen by over 25% in the last ten years by comparison to far smaller increases in off-trade prices, which had largely increased in line with the all items Retail Price Index (RPI), the OFT suggested that in light of the service element involved in the sale of beer in the on-trade, service sector RPI may be a more appropriate comparator.³²⁷ When reliance was placed on this, it was suggested that over the last 10-year period, the real increase in beer prices was only 4%.³²⁸ Proceeding on this basis, the increases in beer prices at the retail level are small and it was suggested that beer prices are not as significant a factor in the on-trade as they once were.³²⁹ The 'offer' to consumers via on-trade premises was 'arguably' improved and there was thought to be a trade-off between this and higher beer prices.³³⁰ In emphasising the reduced importance of price, the range of prices amongst pubs even within a small area, was considered to confirm this increased emphasis on amenity in the UK as a whole.³³¹ This was viewed as an indication that the adverse effects identified by the MMC had been sufficiently reduced to make structural control of the market unnecessary.³³² This was so even although it was

³²² Ibid at para 2.16, p5

³²³ Ibid at para 2.16, p5

³²⁴ Ibid at para 2.16, p5

³²⁵ Ibid at para 2.15, p4. As noted above, the OFT refused to recognise that pubs form a discreet market and instead opted to take a broad view of the relevant market as including all fully on-licensed premises.

³²⁶ Above, n.256 at para 2.15, p4

³²⁷ Ibid at para 4.3, p8

³²⁸ Ibid at para 4.3, p8

³²⁹ Ibid at para 4.4, p8

³³⁰ Ibid at para 4.5, p8

³³¹ Ibid at para 4.5, p8

³³² Ibid at para 4.5, p8

noted that between 1992 and 2000 wholesale prices had fallen by 15% due to the discounts afforded to pubcos by brewers and this had clearly not filtered through to the retail price.³³³

Nevertheless, the price differential between beer and lager was found to have remained despite the costs of production being broadly similar. The OFT however dismissed this as an indication of anti-competitive behaviour as the national brewers suggested their profitability in the sales of lager and beer were similar and given the decline in brewery ownership of public houses, the ale to lager differential was no longer driven by the actions of brewers.³³⁴ The OFT did not however address any possible role played by the pubcos in maintaining this differential. The OFT also turned to consider differences in regional wholesale prices highlighted by the MMC in 1989. These were deemed to have been lessened due to the need for brewers to work from national wholesale price lists following the growth of pubcos which sought to negotiate individual prices for each brand of beer.³³⁵ Consequently such differences were considered to be sufficiently reduced for this to no longer be a competition concern.

2.4.3 Concerns over independence of tied tenants and consumer choice

In addressing the MMC's concerns over the limited independence of pub tenants, reference was made to the European Commission's approval in 1999 of the beer tie agreements of the UK's largest brewers.³³⁶ It was highlighted that whilst Article 101(1) Treaty on the Functioning of the European Union (TFEU) was applicable to these agreements, they benefitted from exemption under Article 101(3) TFEU, and these provisions had not been found to be infringed by the current lease agreements of the major pubcos.³³⁷ It was therefore concluded that none of the agreements underwriting tied tenancies in the UK were anti-competitive and so this was considered sufficient, despite the on-going litigation in the UK between tied tenants and their brewer and pubco landlords, for the OFT to conclude that the competition concerns raised by the MMC over the position of tied tenants no longer remained.³³⁸

Turning to the MMC's concerns regarding the restriction on consumer choice resulting from reliance on beer tie agreements the OFT was unable to state that there had been a significant improvement in this following the Beer Orders. Rather it was noted that "*the*

³³³ Ibid at para 4.6, p9

³³⁴ Ibid at para 4.8, p9

³³⁵ Ibid at para 4.9, p9

³³⁶ See Chapter 3

³³⁷ Above, n.256 at para 4.12, p10

³³⁸ Ibid at para 4.12, p10

choice of beer available to consumers has been at least maintained by brewers”³³⁹ with the choice of on-trade outlet appearing to have increased in importance at the expense of the choice of beers.³⁴⁰ The OFT attributed the maintenance of this level of choice to demands imposed by pubcos enjoying a degree of market power, and responding to consumer preferences. This necessitated brewers supply beers they did not brew including those of smaller brewers.³⁴¹ However, given the limited ability of smaller brewers to compete with the incentives offered to pubcos by the largest brewers to supply their brands discussed above it was acknowledged that smaller brewers still struggled to penetrate the market at the retail level.³⁴²

2.4.4 Brewers’ reliance on the loan tie, the cap on ownership of public houses and the GBP

As mentioned above, brewers’ extensive use of the loan tie had contributed to the MMC’s complex monopoly finding. In reviewing this, the OFT established that due to competition from the commercial banking sector, this was no longer as popular a commercial practice and there was little evidence that it hindered competition.³⁴³ In considering the cap imposed on the number of public houses that could be owned by national brewers under the Tied Estate Order, discussed above, it was acknowledged that its removal could result in brewers re-acquiring large numbers of public houses. This risk was however deemed to be minimal due to the costs involved and because outlets could already be secured by virtue of supply agreements.³⁴⁴ The OFT also suggested that the maintenance of the cap potentially restricted the growth of larger regional brewers.³⁴⁵ Given the significant drop in the number of brewer-owned public houses since the imposition of the cap,³⁴⁶ it was deemed unreasonable to impose significant structural remedies aimed at tackling beer prices, when the majority of pubs were now owned by pubcos and small and independent free traders.³⁴⁷ It was similarly suggested that the GBP discussed above be revoked as they had “*faded into insignificance*”.³⁴⁸ Consequently, the OFT suggested that due to the value

³³⁹ Ibid at para 4.15, p10

³⁴⁰ Ibid at para 4.15, p10

³⁴¹ Ibid at para 4.15, p10

³⁴² Ibid at para 4.16, p10

³⁴³ Ibid at para 4.19-4.20, p11

³⁴⁴ Ibid at para 4.36, p14

³⁴⁵ Ibid at para 4.37, p14

³⁴⁶ As at January 2000, brewers owned 9,770 pubs, by comparison to 34,059 pubs in 1989. Above, n.256 at para 4.38, p14

³⁴⁷ Ibid at para 4.38-4.39, p14-15

³⁴⁸ At that time, they only applied to Whitbread’s tenants and those loan tied to Whitbread, Bass and Scottish and Newcastle. Above, n.256 at para 4.40, p15

now placed by consumers on venue over choice and price, the provisions made little contribution to competition.³⁴⁹

2.4.5 Retention of some provisions of the Beer Orders

In light of the foregoing, despite the lack of any significant improvement in the competitive conditions in the UK beer market and the failure of an independent wholesale sector to emerge, as was deemed central to the success of the Beer Orders, it was concluded that *“the brewing industry and the market for the supply of beer is very different now at all levels of distribution from the 1980s...the changes in the structure and behaviour in the industry appear to have led to an improvement in competition”*.³⁵⁰ This was so even although the primary change was the emergence of the pubco. Although there had been no reduction in retail prices and consumer choice had not improved greatly the OFT stated that *“the concerns which Sir Gordon Borrie had in 1986 about high prices and lack of consumer choice of beer appear to have been diminished.”*³⁵¹ It was therefore recommended that the Beer Orders be revoked, subject to certain provisions regarding loan ties and publication of wholesale prices being retained in an attempt to reduce foreclosure to competing brewers and to maintain the position of independent wholesalers and free houses.³⁵² Despite the many claimed improvements, the OFT was forced to concede that competition in the industry could be better, especially through improved access for competitors, at all levels of distribution, which the Beer Orders alone were unable to achieve.³⁵³ No proposals were however suggested to tackle the remaining anticompetitive issues faced in the market at that time. The Director General simply gave a personal undertaking to ‘be vigilant in his pursuit of anti-competitive practices in the industry and in his consideration of structural changes through mergers’.³⁵⁴ The Government subsequently

³⁴⁹ Ibid at para 4.41, p15

³⁵⁰ Ibid at para 5.4, p16

³⁵¹ Ibid at para 5.4, p16. Gordon Borrie was Director General of Fair Trading when the decision was made to refer the market to the MMC.

³⁵² Provisions of the Loan Tie Order were retained to reduce foreclosure of the market to competing brewers and to maintain the position of independent wholesalers and free trade pubs, namely Article 2 regarding loan tie agreements; Article 4, concerning the publication of wholesale prices; and Article 5, which except in certain circumstances, made the refusal to supply beer for resale unlawful (above, n.256 at para 5.3, p16). While it was acknowledged that wholesale price lists did not reflect the level of discounting that occurred within the industry, the requirement to publish these under Article 4 was thought to impose some restraint on the price discrimination brewers could achieve (ibid at para 4.28, p13). Article 5 was considered to have set an important principle within the industry and was thought to have provided a check on the misuse of power at the wholesale and distribution level by national brewers (ibid at para 4.27, p13).

³⁵³ Above, n.256 at para 5.4, p16

³⁵⁴ Ibid at para 5.5, p16

repealed the Beer Orders in their entirety in 2003 as none of the national brewers to whom they applied remained in tact and so they were no longer relevant.³⁵⁵

3. Conclusion

Having reviewed above the historical development of the British brewing industry, it is apparent that there are numerous links binding the brewing industry and the public house market, with the beer tie being an integral part of the UK's brewing business. Numerous reasons have been identified to explain the UK market, including the need to ensure a constant demand for perishable products and to reduce transportation costs in the early years. However, it is also apparent that the beer tie has been a source of concern throughout the ages as recognised early on by the 1817 Select Committee and latterly, and more controversially, by the MMC. Nevertheless, it has been demonstrated that the resulting Beer Orders were not the most appropriate response to the complex monopoly that existed amongst the Big Six national brewers in the 1980s. The Beer Orders gave rise to numerous unforeseen consequences, including even greater concentration in the industry and the emergence of a tighter and more complex oligopoly than had previously existed. Moreover, foreign multinationals have come to dominate, and with their greater emphasis on powerful branding, have further raised the barriers to entry. However, the most significant consequence was the emergence of the pubco which replaced the brewers in the ownership of substantial tied estates. Thus the Beer Orders were therefore only successful in replacing one set of powerful players with another. The aim of increasing competition in the industry failed to materialise and concerns have continued to be raised over pubcos and their reliance on the beer tie.

The Beer Orders therefore serve as an important warning of the unintended consequences that can arise from interfering in the use of the beer tie which as demonstrated above is largely intertwined into the structure of the UK market and has played an integral role in shaping it. Thus, in order to make recommendations for the reform of regulation of the market, in later chapters some other national markets will be analysed by way of comparison, however, before undertaking such a task it is instructive to consider the application of the EU's competition rules, particularly Article 101 TFEU, to tying agreements.

³⁵⁵ The Supply of Beer (Tied Estate) (Revocation) Order 2002 SI 2002/3204 and The Supply of Beer (Loan Ties, Licensed Premises and Wholesale Prices) (Revocation) Order 2003 SI 2003/52. Above, n.299 at para 24, p12.

Chapter 3 - EU Competition Law and the Brewing Industry

The preceding chapter mapped the historical development of the beer market in the UK and explained why the beer tie remains an integral feature of this market. It also identified why the use of beer tying agreements has attracted considerable and on-going attention from the UK Government and competition authorities. This chapter now examines the application of the competition provisions of the Treaty on the Functioning of the European Union (TFEU) to vertical tying agreements with particular emphasis on those for the distribution of beer.

The chapter provides first an introduction to the EU competition law provisions, with a specific focus on Article 101 TFEU. It touches on the perceived ‘double nature’ of vertical agreements and the impact this has had on the application of the EU competition law provisions to such agreements (Subsection 1). The chapter then focuses on the EU’s evolving approach towards beer supply agreements, briefly noting that the distribution of petrol is the only other sector to be treated by the EU in a similar manner. The emphasis is placed on the provisions of successive block exemption regulations (BERs) the terms of which have been of central importance in the EU’s approach to distribution agreements in the beer market. The decisional practice of the European Commission and Courts is also considered (Subsection 2). Finally, the need for the EU to adopt a more economics-based approach to the handling of vertical agreements is discussed (Subsection 3).

1. Introduction to the EU competition law provisions

EU competition law came into existence on 1 January 1958 and the rules were set out in Articles 85 and 86 of the Treaty of Rome. These are now renumbered Articles 101 and 102 TFEU.¹ The focus of this chapter is Article 101 TFEU, which is concerned with the economic impact of bilateral or multilateral practices as opposed to their legal form.²

Article 101(1) TFEU prohibits “*as incompatible with the internal market*”:

¹ Hereafter referred to as Article 101 and 102 TFEU. For simplicity, the current Treaty numbering is used throughout the thesis in place of preceding Treaty provisions.

² In (Case 56/65) *Société La Technique Minière (STM) v. Maschinenbau Ulm GmbH* [1966] ECR 234; [1966] 1 CMLR 357 at p374 the CJEU held that “[t]o be forbidden as incompatible with the Common Market under Article [101 (1) TFEU], an agreement between undertakings must fulfill certain conditions depending not so much on its legal nature as on its relations, on the one hand, with ‘trade between the [M]ember-States’ and, on the other, with ‘the play of competition’.” Also J Goyder, *EU Distribution Law* 5th Edition (Oxford, Hart Publishing, 2011) at p22-25.

“all agreements between undertakings³ decisions by associations of undertakings and concerted practices which may affect trade between Member States and have as their object or effect the prevention, restriction or distortion of competition within the internal market...”⁴

Article 101(2) TFEU declares such agreements to be automatically void, however Article 101(3) TFEU offers the possibility to save such agreements on satisfaction of its requirements, which generally rely on efficiency grounds as a basis for exception from the prohibition in Article 101(1) TFEU.⁵

By referring to ‘all agreements, decision by associations of undertakings and concerted practices’ Article 101(1) TFEU is wide enough to apply to almost all multilateral conduct, thereby recognising undertakings’ resourcefulness in structuring and describing their arrangements.⁶ It was also expressly confirmed in the seminal case, *Consten & Grundig*⁷ that the prohibition extends to vertical agreements. Whish describes vertical agreements as ‘agreements concluded between operators at different stages of the production and marketing chains’ of a product or service.⁸ As such, beer supply agreements are a form of vertical agreement.

The European Commission at the outset of their application of Article 101(1) TFEU traditionally adopted a formalistic approach to the assessment of agreements between undertakings.⁹ As discussed below, at this time market integration was at the forefront of the Commission’s agenda with it generally assuming that all agreements that were potentially restrictive of competition came within the terms of Article 101(1) TFEU. This approach precluded any economic analysis of the agreement in question until determining

³ The CJEU stated in (Case C-41/90) *Hofnör and Elser v. Macrotron GmbH* [1991] ECR I-1979; [1993] 4 CMLR 306 at para 21, p333 that “...the concept of an undertaking encompasses every entity engaged in an economic activity regardless of the legal status of the entity and the way in which it is financed...” See also R Whish, *Competition Law* 6th Edition (London, Oxford University Press, 2009) at p83

⁴ Article 101(1) TFEU follows with a non-exhausted illustrative list of prohibited practices.

⁵ In order to be offered exception under Article 101(3) TFEU all four of the following requirements must be satisfied by the agreement, decision or concerted practice in question.

“contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

(a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.”

⁶ M Furse, *Competition law of the EC and UK* 6th Edition (Oxford, Oxford University Press, 2008) at p167 and see (Case 56/56) *Société La Technique Minière v. Maschinenbau Ulm* [1966] 1 CMLR 357 at 374

⁷ (Joined cases 56/64 and 58/64) *Etablissements Consten SARL and Grundig-Verkaufs- GmbH v. EEC Commission* [1966] ECR 299; [1966] CMLR 418. This is discussed further below.

⁸ R Whish, *Competition Law* 3rd Edition (London, Butterworths, 1993) at p45 and S Marco Colino, *Vertical Agreements and Competition Law A comparative study of the EU and US Regimes* (Oxford, Hart Publishing, 2010) at p1

⁹ F.M. Carlin, ‘Vertical Restraints: Time for change?’ (1996) 17(5) E.C.L.Rev 283 at 283

whether the requirements of Article 101(3) TFEU were satisfied thereby rendering Article 101(1) TFEU inapplicable. Given the widespread reliance on vertical agreements in the production and distribution of goods throughout the EU, their handling under Article 101 TFEU has been influential in the development and interpretation of the EU competition law provisions.

1.1 Vertical agreements – ‘double nature’ and the development of the EU competition law provisions

As stated above, vertical agreements involve firms operating ‘at different stages of the production and marketing chains of one product’.¹⁰ As such they involve two undertakings that are not competitors and that are not operating on the same relevant market.¹¹ Such vertical agreements are widespread in the distribution and sale of goods and tend to be relied on in the absence of vertical integration.¹² Vertical integration describes the situation where the manufacturer of a product is able to distribute that product through its own distribution chain. In the absence of such integration, and so, where products are distributed by independent undertakings, rather than the manufacturer, vertical agreements replicating the effects of vertical integration are an essential feature of commercial life.¹³ As such, these agreements are widespread in the beer industry, as they are in the petrol industry. As these agreements detail the rights and obligations of the parties, they include ‘restraints’ on the manner in which they can buy, sell or resell goods. Some of these restraints come within Article 101(1) TFEU and are known as vertical restraints.¹⁴ Exclusive purchasing obligations are an example of such a restraint and are widespread within the beer industry as well as the petroleum industry. These restraints generally oblige resellers to acquire the majority of their supplies from a single supplier and not to handle any competing manufacturers’ products.

¹⁰ S Marco Colino, *Vertical Agreements and Competition Law A Comparative Study of the EU and US Regimes* (Oxford, Hart Publishing, 2010) at p1. Also R Whish, *Competition Law* 3rd Edition (London, Butterworths, 1993) at p45.

¹¹ S Marco Colino, *Vertical Agreements and Competition Law A Comparative Study of the EU and US Regimes* (Oxford, Hart Publishing, 2010) at p1

¹² R Whish, *Competition Law* 3rd Edition (London, Butterworths, 1993) at p538

¹³ Above, n.11 at p1. The decision whether or not to vertically integrate is influenced by numerous factors including capital requirements and efficiency gains resulting from using an independent undertaking to distribute goods. Above, n.12 at 537-538. Williamson highlights three categories of motivation for vertical integration as “incentives, controls and what may be referred to as “inherent structural advantages”.” He suggests that the most “distinctive” advantage is the wider variety of control instruments available for enforcing intra-firm activities by comparison with inter-firm activities. Williamson O.E, ‘The Vertical Integration of Production; Market Failure Considerations’ (1971) 61(2) Am Ec Rev 112 at p 113.

¹⁴ Article 1(b) Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (2010) OJ L102/1)

The competitive effects of such restraints largely depend on the market power of the parties to the agreement as well as the prevailing competitive conditions in the relevant market. The competitiveness of a market can be gauged through consideration of the levels of intra-brand competition;¹⁵ and inter-brand competition¹⁶ it supports.¹⁷ The use of vertical restraints can affect inter- and intra-brand competition in the relevant market. Where a manufacturer imposes obligations on the reseller regarding the promotion or sale of his products those obligations will affect the way in which his products are dealt with, thereby only affecting intra-brand competition.¹⁸ Such restrictions tend to be looked on more favorably by the competition authorities than inter-brand restrictions given the manufacturer's genuine interest in the handling of his own products.¹⁹ However, vertical restraints, such as exclusive purchasing obligations which are widespread in the beer market, may affect inter-brand competition by requiring the reseller does not handle the manufacturer's competitors' products.²⁰ The anticompetitive effects of any vertical restraint tends to be reduced where the market is competitive and open as evidenced by the level of inter-brand competition it supports. However, the anticompetitive effects are heightened where there are barriers to entry and the market is foreclosed.²¹ Given the importance of the prevailing market conditions, there are numerous theories highlighting the competitive and anticompetitive effects of vertical agreements.

Wesseling highlights the ambiguous effects of such agreements.²² Exclusive distribution agreements, for example, are a form of vertical agreement that can assist producers in penetrating new markets via incentivised distributors who are protected from the problem of 'free-riding' by other distributors.²³ However, while they can increase both efficiency and inter-brand competition, by offering territorial protection to distributors they can potentially seal off particular geographical markets from others.²⁴ Whilst the beneficial

¹⁵ Competition from retailers of products obtained from the same supplier.

¹⁶ Competition from retailers of products made by a rival producer. V Korah and W.A. Rothnie, *Exclusive Distribution and the EEC Competition Rules Regulations 1983/83 and 1984/83* 2nd Edition (London, Sweet and Maxwell, 1982) at para 1.8, p8.

¹⁷ As Whish notes, competition law is more concerned with restrictions of inter-brand competition than restrictions of intra-brand competition. Restrictions of intra-brand competition only cause concern where inter-brand competition is weak. R Whish, *Competition Law* 6th Edition (London, Oxford University Press, 2009) at p614

¹⁸ Above, n.12 at p45

¹⁹ Ibid at p45

²⁰ Ibid at p45

²¹ Above, n.16 para 1.9, p9 and para 1.11, p11

²² R Wesseling, *The Modernisation of EC Antitrust Law* (Oxford, Hart Publishing, 2000) at p78

²³ Ibid at p78. 'Free riding' occurs where a distributor undertakes the necessary advertising and promotion to penetrate a new market and the manufacturer subsequently supplies its goods to other distributors in the same sales territory who have not incurred the same expenses however benefit by 'free-riding' on the expenditure of the original distributor. See above, n.11 at p20

²⁴ Above, n.12 at p547

effects of such arrangements on inter-brand competition are now recognised, as will be discussed when considering market integration as a goal of EU competition law and the seminal case *Consten & Grundig*, the EU initially veraciously pursued such market partitioning agreements in its application of Article 101 TFEU. By contrast, exclusive purchasing obligations can increase efficiency by allowing manufacturers to have guaranteed outlets for their products thereby enabling them to rationalise production.²⁵ Further, manufacturers may offer financial or other assistance to the resellers subject to such restraints as this will potentially assist in increasing the production of the manufacturer's own goods, not its competitors.²⁶ However, where networks of exclusive purchasing obligations exist, as is the case in the UK brewing industry, this can lead to market partitioning and foreclosure to competing and potential suppliers.²⁷ The exclusive purchasing obligations beer supply agreements impose on resellers essentially deny the supplier's competitors access to those resellers' outlets.²⁸ In the brewing industry, this situation is exacerbated by restrictive licensing which limits the number of available retail outlets in the UK market.²⁹ This has implications for integration and in-store inter-brand competition, whilst also potentially facilitating collusion between suppliers in the case of cumulative use. Further, as exclusive purchasing obligations potentially prevent the reseller from acquiring the same goods elsewhere at a cheaper price, they can ultimately result in the end consumer paying a higher price for the goods in question.³⁰ Consequently Carlin correctly highlights that exclusive purchasing agreements must be clearly defined in scope and limited in duration to avoid this consequence.³¹

In light of the foregoing unpredictable effects and resulting 'double nature' of vertical restraints, Wesseling notes that they have become central to the development of the concept of 'restriction of competition' under Article 101(1) TFEU.³² As discussed above, the European Commission's initially formalistic approach to the application of Article 101(1) TFEU extended to its treatment of vertical agreements with their implications for the competitive and integration processes also driving this approach.³³ Nevertheless, this would soon attract much criticism, most notably from Hawk.³⁴ Hawk highlights the criticisms over the Commission's practice of over-emphasising the importance of intra-

²⁵ Ibid at p542-543

²⁶ Ibid at p543

²⁷ Above, n.22 at p78

²⁸ Above, n.12 at p545

²⁹ Ibid at p545

³⁰ Ibid at p52

³¹ Above, n.9 at p284 and above, n.16 at para 1.9, p9 and para 1.11, p11

³² Above, n.22 at p79

³³ Ibid at p79

³⁴ B.E. Hawk, 'The American (anti-trust) revolution: lessons for the EEC?' (1988) 19(1) E.C.L.Rev 53

brand competition through the strict treatment of export bans, in the pursuit of market integration.³⁵ This largely ignored the distribution efficiencies and increased inter-brand competition that could result from the use of vertical restraints.³⁶ Hawk therefore highlights that resolution of the tensions between the efficiencies resulting from the use of vertical agreements and inter-brand competition; and market integration and distribution concerns has been one of the most significant issues in EU antitrust law.³⁷ Whilst the Commission's approach to vertical agreements is now somewhat more sophisticated, with their benefits being largely accepted, Colino notes that the Commission is still wary of their potential effects,³⁸ with their approach being influenced by the goals of EU competition law, some of which are unparalleled in other antitrust jurisdictions.

1.2 The unique goals of EU competition law

The goals of EU competition law and so the reasoning that informs what competition law should protect is, as Colino notes, influenced by historical and political, as well as social thinking, not to mention economic schools of thought.³⁹ Consequently, certain goals of EU competition law have had greater influence, or find no analogue in other jurisdictions, such as the EU's overarching goal of integration. These goals have impacted on EU policy regarding vertical restraints, which over the past several decades has been criticised and subsequently reformed.

1.2.1 Integration

Although there has been some movement in the order of priority afforded to the goals of EU competition law, with economic efficiency⁴⁰ at the top, due to the historical development of the EU, non-economic goals have also been influential on EU competition policy. These non-economic goals can be understood within a process of integration geared towards the establishment of a single market.⁴¹ As EU competition law has to take into account the constitutional framework provided by the Treaties, a principle objective of

³⁵ Ibid at p74-75

³⁶ Ibid at p74-75. Which also notes the European Commission and Courts' long-held concerns over market partitioning, even where the restrictions in question concern intra-brand competition as opposed to inter-brand competition. Above, n.17 at p614.

³⁷ Above, n.34 at p75

³⁸ Above, n.11 at p15

³⁹ Ibid at p25 and p28

⁴⁰ Motta notes social welfare is also taken into consideration in EU competition policy. He highlights that social and political considerations influence the way in which competition policy is implemented. Competition may therefore be "*sacrificed*" where the social costs of it are considered to be too high, for example where significant job losses would result. M Motta, *Competition Policy Theory and Practice* (Cambridge, Cambridge University Press, 2004) at p15.

⁴¹ Above, n.11 at p25 and p27

competition law was, and to a more limited extent today is, integration through the eradication of discrimination based on national grounds.⁴² Consequently, the competition regime under the TFEU has a strong emphasis on opening up markets to competition. As a result, the Commission was initially keen to condemn firms' attempts to segment national markets, for example by conferring absolute territorial protection on resellers.⁴³ This subsequently impacted on the treatment of vertical restraints which vary significantly in scope. As Whish highlights, such restraints raise many 'complex theoretical and analytical problems'⁴⁴ with their mixed effects requiring individual attention to determine their competitive impact.⁴⁵ Nevertheless, due to their 'double nature' stated above, and the risk they pose to market integration, vertical agreements have been subject to a high degree of regulatory intervention under EU competition law.⁴⁶

1.2.2 Economic Freedom

As stated above, economic efficiency may have greater primacy today as a goal of EU competition law however this was not always the case. When EU competition law rules were adopted, the thinking of German Ordoliberal scholars, known as the 'Freiburg School', which advocated 'the economic freedom of action of all actors,' significantly influenced the development of European competition law.⁴⁷ They sought to keep government power in check in order to protect individual freedoms whilst also recognising the need for the State to be strong enough to resist the misuse of private power.⁴⁸ The notion of economic freedom subsequently came to be a goal of EU competition law. Given the desire to facilitate open markets and ensure economic freedom,⁴⁹ vertical restraints were subject to a high level of interference by the EU competition authorities.⁵⁰ As Colino notes, the Commission attached itself to the concept of 'economic freedom' and considered the concept of 'restriction of competition' as the negative effects deriving from a restriction on the economic freedom of the operators in the market.⁵¹ As a result, almost all

⁴² Above, n.40 at p14

⁴³ Ibid at p14

⁴⁴ Above, n.12 at p536

⁴⁵ Above, n.11 at p26

⁴⁶ Above, n.22 at p78-79 and above, n. 34 at p73

⁴⁷ D.J. Gerber, *Ordoliberalism: A New Intellectual Framework for Competition Law*, (Oxford Scholarship Online, 2010) at p232 and A Weitbrecht, 'From Freiburg to Chicago and beyond – the first 50 years of European Competition Law' (2008) 29(2) E.C.L.Rev 81 at 82

⁴⁸ D.J. Gerber, *Ordoliberalism: A New Intellectual Framework for Competition Law* (Oxford Scholarship Online, 2010) at p240. G Amato, *Antitrust and the Bounds of Power* (Oxford, Hart Publishing, 1997) at p39-41

⁴⁹ D J. Gerber, *Ordoliberalism: A New Intellectual Framework for Competition Law* (Oxford Scholarship Online, 2010) at p249

⁵⁰ Above, n.40 at p24

⁵¹ Above, n.11 at p61

agreements were prohibited under Article 101(1) TFEU.⁵² This was due to the fact that a party's freedom to act is almost always limited on entering a contractual arrangement, as exemplified by beer supply agreements which contain exclusive purchasing obligations.⁵³ However, this approach would ultimately distinguish the EU from other antitrust jurisdictions, such as the United States, where in the 1980s, the Chicago School was influential. By contrast to the Freiburg School, the Chicago School advocated economic efficiency as the only goal of antitrust and pointed to the efficiency enhancing qualities of vertical restraints, including their ability to enhance inter-brand competition.⁵⁴ Consequently, as already stated above, the initial lack of economic analysis in the Commission's decisions and its attachment to the notion of economic freedom caused its policies on vertical restraints to be one of the most criticised aspects of EU competition policy.⁵⁵

1.2.3 Protection of small and medium sized enterprises

Another goal of EU competition law, once shared by the United States,⁵⁶ is the protection of small and medium sized enterprises (SMEs).⁵⁷ As Colino notes, this has its basis in the neoclassical economic belief that the greater the number of competitors in the market, the more intense competition will be.⁵⁸ However, Motta highlights that while resources should not be expended on monitoring the agreements of small firms, their over-protection through attempts to address the issues faced by SMEs may cause distortions in the competitive sphere.⁵⁹ Nevertheless, the goal of protecting SMEs is evident in the EU's *de minimis* doctrine, developed in *Völk v Vervaecke*.⁶⁰ This doctrine clarifies what is not considered to be an appreciable restriction of competition for the purpose of the application of Article 101(1) TFEU. This has been supplemented by a series of Notices issued by the European Commission over the past several decades.⁶¹ As will be discussed below, in

⁵² Ibid at p61

⁵³ Above, n.22 at p78-79

⁵⁴ Above, n.34 at p57 and above, n.11 at p20

⁵⁵ B Hawk, 'System Failure: Vertical Restraints and EC Competition Law' (1995) 32(4) C.M.L.Rev 973 at 977-978 and above, n.11 at p60-61

⁵⁶ US antitrust law came into being following complaints from small enterprises against large trusts in the 19th Century. Above, n.40 at p22

⁵⁷ Hereinafter referred to as SMEs

⁵⁸ Above, n.11 at p32

⁵⁹ Above, n.40 at p22. Motta highlights that assisting small firms to survive when they are unable to operate at an efficient scale of production would cause the inefficient allocation of resources and would ultimately contribute to higher prices in the economy (ibid at p22).

⁶⁰ Case 5/69 [1969] ECR 295

⁶¹ The first notice was European Commission, *Notice on Agreements of Minor Importance* ((1970) OJ C64/1). (No English translation available) The current notice is European Commission, *Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty Establishing the European Community (de minimis)* ((2001) OJ C368/13)

applying the *de minimis* doctrine to the UK beer market, the European Commission came to distinguish the beer tie agreements of national brewers from those entered into by small regional brewers. It considered that the former foreclosed the market thereby requiring individual examination, whilst the latter, on account of the size of the breweries concerned were out with the scope of Article 101(1) TFEU, except where their cumulative effect was foreclosure or hindered market access.⁶²

2. The EU's evolving approach towards beer supply agreements

For the reasons stated above, the terms of Article 101 TFEU, the perceived 'double nature' of vertical agreements and the goals of EU competition law, have all impacted on the EU's policy decisions affecting vertical agreements, including the vast number in the beer industry. Another industry which has been affected by these policy decisions is the petrol industry, which is significantly similar to the beer industry in that it shares a distinct prevalence for such agreements. This is explained by Whish who highlights the natural tendency towards vertical integration within these markets.⁶³ As stated above, vertical restraints can be used to replicate the effects of vertical integration. This is possible as they align the objectives of the parties to the agreement, with this being preferred when large sums have been invested in public houses and service stations, as is commonly the case in these industries.⁶⁴ Nevertheless, in charting the EU's evolving approach towards beer supply agreements and the vertical restraints contained within them, the focus will be placed on the provisions of the various Block Exemption Regulations (BERs) that have been adopted over the decades. This is due to the fact that historically, most agreements within this market were drafted to come within the terms of a BER due to the Commission's overly-broad and formalistic application of Article 101(1) TFEU discussed above. However, regard will also be had to the relevant decisions of the European Commission and of the European courts, including those which provided guidance on the assessment of vertical agreements prior to the adoption of the first BER in 1967 which are still of importance today.

2.1 Pre-Block Exemption Regulations

Prior to the adoption of the first BER in 1967, guidance on assessing the legality of agreements was to be gleaned from the decisional practice of the European Commission

⁶² D.A. Cowan and J.S. Nazerali, 'Beer Supply Agreements – a Step Forward of Last Orders?' (1998) 19(5) E.C.L.Rev 289 at 290

⁶³ Above, n.12 at p538

⁶⁴ Above, n.40 at p303-304 and R.J. Van den Bergh and P.D. Camesasca, *European Competition Law and Economics: A Comparative Perspective* 2nd Edition (London, Sweet & Maxwell, 2006) at p207

and Courts, with quite clear instruction being provided in the 1966 case *Société Technique Minière*.⁶⁵ There the Court of Justice of the European Union (CJEU) clarified that the words ‘object or effect’ in Article 101(1) TFEU were to be read disjunctively.⁶⁶ It stated that “[t]he fact that these are not cumulative but alternative conditions, indicated by the conjunction ‘or’, suggests first the need to consider the very object of the agreement...”⁶⁷ In applying this, it firstly has to be determined whether the agreement has the object in its economic context to restrict, distort or prevent competition; and secondly, if this consideration of the object of the agreement fails to show a “sufficient degree of harmfulness with regard to competition”, it has to be determined whether it has an appreciable effect on competition through an examination of the relevant facts.⁶⁸ It therefore highlighted at an early stage the importance of the economic context in determining the purpose of an agreement. The European Commission, however, was slow to follow this approach.⁶⁹ This was significant as the European Commission, by virtue of Article 9 of Regulation 17/62,⁷⁰ enjoyed the exclusive right to declare Article 101(1) TFEU inapplicable to an agreement on the basis of Article 101(3) TFEU. It therefore effectively enjoyed a monopoly in applying Article 101 TFEU, to the exclusion of the national courts and competition authorities.⁷¹ The only means of ensuring exemption of an agreement was to notify the European Commission, causing it to be inundated with agreements but also presenting an opportunity for it to further the goal of integration through its decisional practices.⁷²

2.1.1 Influence of *Consten & Grundig*

At a time when integration was at the forefront of the European Commission’s priorities, it was empowered by its virtual monopoly under Regulation 17/62 in the application of Article 101 TFEU, to control those restraints that threatened to divide the common market.⁷³ Due to the wide scope afforded to the notion of restriction of competition, and its reluctance to recognise that certain restraints could divide the market, whilst also

⁶⁵ (Case 56/65) *Société Technique Minière (STM) v Maschinenbau Ulm* [1966] ECR 234; [1966] 1 CMLR 367

⁶⁶ (Case 56/65) *Société Technique Minière (STM) v Maschinenbau Ulm* [1966] C.M.L.R. 357 at 375

⁶⁷ *Ibid* at 375

⁶⁸ *Ibid* at 375. D Weston and J Pheasant, ‘Vertical Restraints, Foreclosure and Article 85 Developing an analytical framework’ (1997) 18(5) E.C.L.Rev 323 at 324

⁶⁹ Above, n.11 at p65

⁷⁰ Regulation No 17 First Regulation implementing Article 85 and 86 of the Treaty ((1962) OJ 13/204)

⁷¹ A Weitbrecht, ‘From Freiburg to Chicago and beyond – the first 50 years of European Competition Law’ (2008) 29(2) E.C.L.Rev 81 at 82. Above, n.11 at p62. Colino notes that this monopoly allowed the Commission to ensure uniformity in the application of the competition law provisions.

⁷² Above, n.11 at p62

⁷³ *Ibid* at p62

enhancing competition, most agreements were found to infringe Article 101 TFEU.⁷⁴ In the seminal 1960s case of *Consten & Grundig*⁷⁵ the Commission, as endorsed by the CJEU, clarified the application of Article 101 TFEU to vertical agreements.⁷⁶ The general concern was that such agreements could isolate markets by re-establishing barriers to trade along national lines, thereby frustrating the basic objects of the EU. The CJEU stated that the preamble and text of the Treaty is aimed at “*suppressing the barriers between States and...could not allow undertakings to restore such barriers.*”⁷⁷ It reaffirmed that Article 101 TFEU was intended to prohibit this even where the agreement concerned undertakings “*placed at different levels of the economic process*”, as in vertical arrangements.⁷⁸ Consequently, an exclusive distribution agreement between the parties, which made provision for absolute territorial protection for Consten supported by the grant of an exclusive licence of the Grundig trademark throughout the territory of France, was contrary to the internal market philosophy and was prohibited.⁷⁹ As Wesseling notes, by holding that an agreement which aims to separate artificially national markets for certain goods, thereby hindering the free movement of goods is a restriction of competition, the CJEU linked the concept of competition under EU competition rules to the process of market integration.⁸⁰ Further, in keeping with its earlier decision in *Société Technique Minière*,⁸¹ discussed above, as the agreement appeared to have the object of restricting, preventing or distorting competition, it was prohibited without the need to assess the actual effects of the agreement.⁸² Consequently, *Consten & Grundig* clarified the application of Article 101 TFEU, to vertical agreements, and reinforced the principles driving its

⁷⁴ Ibid at p61

⁷⁵ Joined Cases, 56/64 and 58/64 *Etablissements Consten SARL & Grundig-Verkaufs GmbH v. Commission* [1966] ECR 299, [1966] CMLR 418

⁷⁶ As noted by Weitbrecht the CJEU at this time, assumed a supporting role for the Commission’s integration agenda. A Weitbrecht, ‘From Freiburg to Chicago and beyond – the first 50 years of European Competition Law’ (2008) 29(2) E.C.L.Rev 81 at 83

⁷⁷ Joined Cases, 56/64 and 58/64 *Etablissements Consten SARL and Grundig-Verkaufs GmbH v. Commission* [1966] C.M.L.R. 418 at p471

⁷⁸ Ibid at p471

⁷⁹ The CJEU, however, in-keeping with its earlier decision in *Société Technique Minière*, did not accept that exclusivity clauses alone would automatically cause an agreement to breach Article 101(1) TFEU. The clauses considered incompatible with Article 101(1) TFEU were those concerning absolute territorial protection and the agreement concerning the Grundig trademark (above, n.77 at 474-475.)

⁸⁰ Above, n.22 at p85

⁸¹ Above, n.66. STM had been granted exclusive rights to sell machines in France and some overseas territories. When Maschinenbau did not receive payment, it sued STM which in turn claimed that some of the clauses under the agreement were void under Article 101(1) TFEU. The CJEU however took the view that such agreements could normally benefit from exemption under Article 101(3) TFEU. It stated that “*the alteration of the conditions of competition may be thrown in doubt if the said agreement appears precisely necessary for the penetration of an undertaking into an area in which it was not operating*”. (Above, n.66 at p375)

⁸² Above, n.77 at p471 and p473

application most notably market integration. The decision in *Consten & Grundig* was closely followed by the Commission in the drafting of Regulation 67/67.⁸³

2.2 The Block Exemption Regulations

BERs are ‘self-regulatory mechanisms’, in that, should their terms be fully complied with, the parties to an agreement, can be satisfied that the agreement complies with EU competition law.⁸⁴ However, the Commission’s early BERs were subject to much criticism for adopting a highly formalistic approach.⁸⁵

2.2.1 Regulation 67/67 – the starting point

The first BER was adopted in 1967 to stem the flow of agreements besieging the European Commission seeking an individual exemption under Article 101(3) following the adoption of Regulation 17/62⁸⁶ and the *Consten & Grundig* judgment.⁸⁷ The new BER reflected the desire to filter out those agreements which although *prima facie* contrary to Article 101(1) TFEU had overall pro-competitive effects.⁸⁸ In doing so, Regulation 67/67 acknowledged the benefits of exclusive dealing arrangements, including their ability to bring about improvements in the distribution of goods.⁸⁹ Article 1 of Regulation 67/67 detailed the exemption. This applied to exclusive distribution and purchasing agreements⁹⁰ between two undertakings, where these were concerned with goods for resale, but not services.⁹¹ Although there were no express rules governing beer supply agreements, by including exclusive purchasing agreements, they were implicitly included within the terms of Regulation 67/67. However, Article 1(2) of Regulation 67/67 provided that agreements

⁸³ Commission Regulation (EEC) No 67/67 of 22 March 1976 on the application of Article 85(3) of the Treaty to certain categories of exclusive dealing agreements ((1967) OJ (spec ed) 10). R Greaves, *EC Block Exemption Regulations* (London, Chancery Law Publishing, 1994) at p50

⁸⁴ Above, n.17 at p164

⁸⁵ Above, n.11 at p64

⁸⁶ Above, n.70

⁸⁷ Above, n.77

⁸⁸ N .J. Sarad ‘EEC Regulation of Exclusive Dealing Arrangements’ (1985-1986) 3 Int’l Tax & Bus. Law. 81 at 83

⁸⁹ Recital 6 of Regulation 67/67. It was also during this period when the Commission was seeking to reduce the amount of time it had to allocate to the consideration of notifications and complaints of anticompetitive behaviour that it published its first Notice on Agreements of Minor Importance (*de minimis*) (1970) OJ C64/1. In order to stem the flow of agreements to the Commission this clarified the rules under which agreements of minor importance would not infringe Article 101 TFEU. G Monti, *EC Competition Law* (Cambridge, Cambridge University Press, 2007) at p397-398

⁹⁰ Green states the principal distinctions to be drawn between exclusive distribution and exclusive purchasing agreements are that, in the former, the dealer is allocated an exclusive territory within which he has the contractual right to sell the supplier’s brand of goods. In the latter, no exclusive territory is allocated with the supplier enjoying the freedom to enter into agreements with other dealers in the same territory, however, the dealer is obligated to take supplies exclusively from that supplier. N Green, *Commercial Agreements and Competition Law practice and Procedure in the UK and EEC* (London, Graham & Trotman, 1986) at p471

⁹¹ R Greaves, *EC Block Exemption Regulations* (London, Chancery Law Publishing, 1994) at p50

where the undertakings were from one Member State and concerned the resale of goods within that State, were excluded as they rarely affected trade between member states. This effectively rendered the BER inapplicable to UK national beer agreements as both parties were from the same Member State.⁹²

However, in the same year as Regulation 67/67 was adopted, the CJEU provided guidance on beer agreements in *Brasserie de Haecht*.⁹³ In a preliminary ruling concerning the compatibility of a beer supply agreement with Article 101(1) TFEU, the Court confirmed that such agreements could be caught by Article 101(1) TFEU however, it was unlikely that a beer agreement incorporating an exclusive purchasing obligation would restrict competition by object.⁹⁴ The CJEU clarified that where an agreement does not have the object of restricting competition, it is necessary to perform an extensive analysis of its effects in order to determine whether it restricts competition.⁹⁵ It stated that “[t]o judge whether it is hit by Article [101](1), a contract can thus not be isolated from that context, i.e., from the factual or legal circumstances resulting in it having the effect of preventing, restricting or distorting competition. With regard to that objective, the existence of similar contracts can be taken into account in so far as all the contracts of that type as a whole are such as to restrict the freedom of trade.”⁹⁶ The guidance provided by the CJEU was therefore that the effect of the beer supply agreement in question had to be considered in its complete legal and economic context, highlighting the importance of assessing the restraint, not in the abstract, but within the context in which it operates, in order to determine its effects.

Whilst the judgment of the CJEU in *Brasserie de Haecht* suggested it was adopting a more economics based approach to the assessment of vertical agreements under Article 101(1) TFEU, this was not reflected in the terms of Regulation 67/67. In keeping with the desire for legal certainty, Article 2 of Regulation 67/67 detailed a ‘White’ list of permissible restrictions which could be placed on the exclusive dealer if exemption was to be secured. The Regulation also provided in Article 3 a ‘Black’ list of clauses which would deny the agreement an automatic exemption from the prohibition of Article 101(1) TFEU. Consequently, the Regulation was largely formalistic with all agreements having to be drafted to include the permitted ‘White’ clauses, whilst excluding those outlawed by the

⁹² Article 1 and Recital 4 of Regulation 67/67. Also ‘British and European Community regulation of the British Beer Market: Tapping into the tied house system (Cheers!)’ (1990) 20 Ga. J. Int’l & Comp. L. 583 at 590

⁹³ (Case 23/67) *Brasserie de Haecht v. Wilkin and another* [1967] ECR 407; [1968] CMLR 26

⁹⁴ (Case 23/67) *Brasserie de Haecht v. Wilkin and another* [1968] CMLR 26 at p41.

⁹⁵ *Ibid* at para 4, p40

⁹⁶ *Ibid* at para 4, p40

‘Black’ list. In line with the internal market philosophy, the ‘Black’ list respected the ‘cardinal rule’ of no absolute territorial protection and sought to ensure intra-brand competition was preserved.⁹⁷ While this approach satisfied the need for legal certainty, it denied undertakings the freedom to draft agreements on the basis of commercial considerations and overlooked the economic effects of the agreements in question. Nevertheless, the format set by Regulation 67/67 was followed by its successors,⁹⁸ which were later criticised for their ‘straitjacket effect’ on agreements and for their lack of economic analysis.⁹⁹

2.2.1.1 Extension of Regulation 67/67

Whilst agreement was being reached on the terms of Regulation 67/67’s successor, the BER had to be amended to accommodate the CJEU judgment in *Fonderies Roubaix – Wattrelos v. Fonderies Roux*.¹⁰⁰ The judgment confirmed that Regulation 67/67 did in fact cover agreements which satisfied its requirements even where the parties were based in the same Member State,¹⁰¹ with this being reaffirmed in *Concordia*.¹⁰² These judgments therefore opened up the possibility of exemption to beer and service station agreements involving parties in one Member State.¹⁰³ However, at this time between the extension of Regulation 67/67 and the adoption of its successors, the Commission had been notified of far more agreements concerning the supply of beer than petrol, but had avoided taking a formal decision on a brewery contract. Instead, it opted to pursue enquiries into the industry under Article 12 of Regulation 17/62, and Sinan notes that during these evaluations, brewery contracts benefitted from a “*relatively liberal application of the EEC competition rules*”.¹⁰⁴ This was despite the fact that in the UK, concern was being expressed about the increasing width of the beer tie which now included, amongst others, wines, sprits, soft drinks and amusement machines.¹⁰⁵

⁹⁷ Above, n.9 at 248

⁹⁸ Above, n.91 at p50

⁹⁹ European Commission, *Communication from the Commission on the application of the Community competition rules to vertical restraints (Follow-up to the green paper on vertical restraints)* ((1998) OJ C365/3) at para 4, 23

¹⁰⁰ Case 63/75, *Fonderies Roubaix – Wattrelos v. Fonderies Roux* [1976] ECR 111 at 118

¹⁰¹ Article 1(2) of Regulation 67/67. See above, n.91 at p51

¹⁰² (Case 47/76), *De Norre v. N.V. Brouwerij Concordia* [1977] ECR 65. This concerned a loan by the Concordia brewery in exchange for the recipients and their successors undertaking that their café would purchase only Concordia products

¹⁰³ Ibid. See also I.M. Sinan, ‘Tied House Agreements and the EEC Competition Rules: A Brief History’ (1985) N.L.J. 25 October 1063 at 1063 and D.G. Goyder, *EC Competition Law* 2nd Edition (Oxford, Clarendon Press, 1993) at p226-227

¹⁰⁴ I.M. Sinan, ‘Tied House Agreements and the EEC Competition Rules: A Brief History’ (1985) N.L.J. 25 October 1063 at 1063

¹⁰⁵ Written question No 2187/82 ([1983] OJ C266/2) at question 1, p2

2.2.2 The need for more than one regulation

The European Commission opted to replace Regulation 67/67 with two BERs, which would operate alongside the 1977 Notice on Agreements of Minor Importance (1977 Notice).¹⁰⁶ The decision to adopt two BERs was partly attributed to the CJEU's aforementioned judgment in *Concordia*. This judgment did not just reaffirm that Regulation 67/67 was applicable to agreements that satisfied its requirements even where the parties were based in the same Member State, but clarified other aspects of its application. Whilst Article 1 of Regulation 67/67 did not impose a requirement for an exclusive purchasing agreement to specify an exclusive territory to gain exemption¹⁰⁷ as Korah and Rothnie note, the Commission appears to have considered one of these requirements to be the counterparty of the other.¹⁰⁸ From a literal reading of the provision it is unclear why the Commission would have done so. However, Korah and Rothnie seek to justify this on the basis of the Commission being more concerned than the Court that exclusive purchasing obligations may have the effect of foreclosing too much inter-brand competition.¹⁰⁹ This explanation is in line with the Commission's practices discussed above. The Commission subsequently highlighted this judgment and the lack of any provisions in Regulation 67/67 dealing with the specific issues arising from exclusive purchasing agreements as justification for the need to adopt two separate BERs.¹¹⁰

These ultimately came in the form of Regulations 1983/83 on exclusive distribution agreements, and Regulation 1984/83 dealing with exclusive purchasing agreements.¹¹¹ The Commission stated that the adoption of two BERs was preferred due to the "*differences in the nature of such agreements and in their implications for competition in the common market*".¹¹² The Commission noted that exclusive distribution agreements and the allocation of exclusive sales territories to resellers may result in market partitioning and a substantial lessening in intra-brand competition.¹¹³ By contrast, the Commission

¹⁰⁶ It provided a qualitative test of turnover, and a market share test requiring that the products subject to the agreement do not represent in a substantial part of the Common Market more than 5% of the total market for such products. European Commission, *Notice of 19 December 1977 concerning agreements of minor importance which do not fall within Article 85(1) of the Treaty establishing the European Economic Community* ((1977) OJ C313/3). Also above, n.90 at p242.

¹⁰⁷ Above, n.91 at p51

¹⁰⁸ Above, n.16 at para 3.1, p59

¹⁰⁹ Ibid at para 3.1, p59

¹¹⁰ European Parliamentary Question No. 1764/82 ([1983] C93/22) at answer at para 1(a), 23

¹¹¹ A third Regulation – Commission Regulation (EEC) No 4087/88 of 30 November 1988 on application of Article 85(3) of the Treaty to categories of franchise agreements OJ (1988) L359/46 was adopted to deal with franchising. This will not be discussed here.

¹¹² Commission of the European Communities, *Thirteenth Report on Competition Policy* (1984, Brussels) at para 27, p36

¹¹³ Ibid at para 27, p36

highlighted that exclusive purchasing agreements presented the problem of market foreclosure to competing manufacturers and suppliers thereby limiting inter-brand competition in the EU.¹¹⁴ This was considered to be particularly likely where there is a network of similar contracts affecting the largest or majority of retail outlets.¹¹⁵ The Commission sought to define specific rules for beer supply agreements in light of the ability of a network of such agreements to “*immobilize competitive structures within the national markets affected and to partition off these markets, because they make it much more difficult for suppliers from other Member States to distribute their products through the established public houses, cafes and so on.*”¹¹⁶ These concerns prompted the Commission to express its intention not to deny such agreements exemption but to use the new provision to ‘loosen’ the exclusive purchasing obligations that could qualify for exemption from the EU competition law provisions.¹¹⁷ Therefore given the significance of the new provisions of Regulation 1984/83 in order to gain exemption for beer supply agreements, this chapter will focus on its terms, not those of the exclusive distribution BER.

2.2.3 Regulation 1984/83

In adopting the new BERs, the Commission intended to “*bring the rules applicable to these types of agreements into line with developments both in the economic reality of the common market and in Community competition law*”.¹¹⁸ In adopting Regulation 1984/83 on exclusive purchasing agreements, the Commission states that its underlying rationale was “*agreements of this kind covering the purchase of goods for resale display similar features in almost all sectors of the economy, so that they can be brought under a common set of rules*”.¹¹⁹ However, the Regulation was also the first time that the Commission had drafted provisions specifically dealing with exclusive purchasing agreements within the brewing industry. The only other sector selected for similarly special handling under the Regulation was the petrol industry. It stated that “[*b*]rewery and filling station agreements, however, show clear differences from other exclusive purchasing agreements so that special rules were necessary for those sectors”.¹²⁰ Whilst this may have been so, it has also been suggested that the vast number of beer and service station agreements in force across the EU at that time was influential. The Commission was made aware of the substantial

¹¹⁴ Ibid at para 27, p36

¹¹⁵ Ibid at para 27, p36

¹¹⁶ Above, n.110 at answer at para 1(a), 23

¹¹⁷ Ibid at answer at para 1(a), 23

¹¹⁸ Above, n.112 at para 27, p36

¹¹⁹ Ibid at para 29, p37

¹²⁰ Ibid at para 29, p37

opposition that would arise from brewery interests in several Member States should they be prohibited from relying on their existing long-term exclusive purchasing obligations.¹²¹ Consequently, the preamble to Regulation 1984/83 stated that following the Commission's experience three categories of agreement and concerted practices were regarded as satisfying the conditions of Article 101(3) TFEU. These are noted in the BER as exclusive purchasing agreements of short and medium duration in all sectors of the economy; long-term exclusive purchasing agreements entered into for the resale of beer in premises used for sale and consumption, being beer supply agreements; and of petroleum products in service stations, being service station agreements.¹²² Consequently, the Regulation was divided into three Titles, one for each category of agreement. Titles I and II will be discussed here while Title III is discussed in greater depth in Chapter 6.

2.2.3.1 Title I of Regulation 1984/83 – exclusive purchasing agreements in all sectors of the economy

Title I was concerned with exclusive purchasing agreements in all sectors, and followed the same mechanistic format of Regulation 67/67 by detailing the exemption and providing 'white' and 'black' lists of restraints. Consequently, Article 1 stated that exemption was only open to bilateral agreements for the purchase of certain goods specified in the agreement for resale, not services. However, in light of the CJEU rulings discussed earlier in *Foundaries Roubaix and Concordia*, no mention was made of the undertakings being required to be in the same Member State or for a geographical area to be specified in the agreement.¹²³ Article 2 detailed the 'white' list. This stated that the only permissible restriction that could be imposed on the supplier was the obligation not to distribute the contract goods or competing goods in the reseller's principal sales area, namely the area covered by their "*normal business activity*",¹²⁴ and at the reseller's level of distribution. Article 2(2) added to this that the only permissible restriction on the reseller was an obligation not to manufacture or distribute goods, which compete with the contract goods, although Article 2(3) provided certain exceptions to this through the provision of an exhaustive list of restrictions which could be imposed on the reseller. Article 2(3) permitted an obligation on resellers to purchase complete ranges of goods, and differed from Regulation 67/67 by permitting an obligation to purchase a minimum quantity of the

¹²¹ D.A. Evereste, 'British and European Community regulation of the British Beer Market: Tapping into the tied house system (Cheers!)' (1990) 20 Ga. J. Int'l & Comp. L. 583 at 610

¹²² Recital 2 of Regulation 1984/83

¹²³ Recital 3 and Article 1 of Regulation 1984/83

¹²⁴ European Commission, *Notice concerning Commission Regulations (EEC) No 1984/83 and (EEC) No 1983/83 of 22 June 1983 on the application of Article 85(3) of the Treaty to categories of exclusive distribution and exclusive purchasing agreements* ((1984) OJ C 101/2) at para 37, 7

goods subject to the exclusive purchasing obligation.¹²⁵ These white list obligations were considered to compel resellers to focus their sales efforts and were deemed necessary to improve the distribution of goods subject to the exclusive purchasing obligation.¹²⁶ They were, however, limited to the duration of the agreement and no further restrictions could be imposed.¹²⁷ Article 3 followed with the ‘black’ list. This prohibited exclusive purchasing agreements between competing manufacturers;¹²⁸ precluded exclusive purchasing obligations for unconnected goods, thereby attempting to limit the obligation to take complete ranges under Article 2(3)(a).¹²⁹ It further prohibited agreements for an indefinite duration or more than five years. Consequently Article 3 reflected the principle of the Regulation that market foreclosure is directly connected with the duration and scope of the exclusive purchasing obligation.¹³⁰ Article 14 also made provision for the withdrawal of the benefit of the BER from agreements under any Title where, among others, the contract goods were not subject to effective competition from identical or equivalent goods “*in a substantial part of the common market*”.¹³¹ However, the most significant departure from Regulation 67/67 was the inclusion of specific rules regarding beer and petrol supply agreements in Titles II and III of the Regulation.

2.2.3.2 Beer supply agreements under Regulation 1984/83

During the consultation period informing Regulation 1984/83, the European Commission was convinced that purchasing agreements within the beer and petrol sectors were distinct on account of the way the products within these were sold and distributed. This was due to the fact that unlike any other sector, on account of the large capital outlays often involved, breweries and oil companies would frequently buy and lease premises to resellers or almost always finance the acquisition of sites.¹³² However, this investment also benefitted suppliers due to the importance afforded to brand preference within these sectors with such expenditure on retail outlets encouraging brand loyalty.¹³³ Consequently, the Regulation emphasised that beer and service station agreements merited distinct rules to take into account the ‘peculiarities of the markets in question’ with provision being made to

¹²⁵ Article 2(3) Regulation 1984/83

¹²⁶ Recital 8 of Regulation 1984/83

¹²⁷ Recital 8 of Regulation 1984/83. It was expressly stated that further restrictions, and in particular those which limit the reseller’s choice of customers or his ability to determine the price and conditions of sale of the goods, could not be exempted under the Regulation

¹²⁸ Article 3(a) Regulation 1984/83. This ensured inter-brand competition was not reduced

¹²⁹ Article 3(c) Regulation 984/83. Also above, n.124 at para 38, 7

¹³⁰ Article 3 Regulation 1984/83. Also above, n.112 at para 29, p37

¹³¹ Article 14(a) Regulation 1984/83

¹³² Above, n.91 at p54

¹³³ Ibid at p54. As will be discussed in Chapter 6, brand preference is no longer a feature of the UK petrol market due to the scrapping of the star rating system for fuel. Petrol is now deemed to be a homogeneous product. Due to beer’s heterogeneous quality, brand preference remains a significant feature of the market

preclude the combination of the different Titles under the Regulation.¹³⁴ Nevertheless, Korah and Rothnie highlight that the new sector-specific rules were too interventionist and failed to consider fully economic considerations, with very similar provisions being enacted to deal with both industries.¹³⁵ The rigidity of the rules is plainly evident from a simple reading of Regulation 1984/83.

2.2.3.3 Title II– Special Provision for Beer

Recital 13 sought to justify the decision to implement distinct rules for agreements in the beer and petrol markets. This further emphasised the fact that in contrast to other exclusive purchasing agreements, in these sectors the supplier often confers on the reseller ‘special commercial or financial advantage’. The Commission shed some light on what was required in order to confer such an advantage on a reseller stating that this goes “*beyond what the reseller could normally expect under an agreement*”.¹³⁶ Recital 13 of the BER provided examples of this, again, referring to ‘the granting of loans on favourable terms, and the provision of business premises’. The BER also highlighted that, as with other exclusive distribution agreements, such agreements in these sectors result in an appreciable improvement in distribution, with consumers enjoying a fair share of the resulting benefit.¹³⁷

In light of the foregoing justifications, beer agreements were exempted under Article 6(1) of Regulation 1984/83. The Regulation offered exemption where the agreement concerned two undertakings and the reseller agreed with the supplier, in consideration for according of special commercial or financial advantages, to purchase only from the supplier, certain beers or certain beers and certain other drinks, specified in the agreement for resale in the premises, used for the sale and consumption of drinks and designated in the agreement.¹³⁸ The crux of Article 6 was therefore that for exemption to be granted, the exclusivity must be in consideration of special commercial or financial advantage granted by the supplier.¹³⁹ The Commission considered that this made it significantly easier for resellers to establish, operate and maintain their premises, whilst the ban on dealing in competing goods provided the necessary motivation to concentrate on the sale of the contract goods.¹⁴⁰ This

¹³⁴ Article 17 precluded the exemption from applying to mixed agreements – an exclusive purchasing agreement which spanned more than one Title did not qualify for exemption. Above, n.90 at p478.

¹³⁵ Above, n.16 at para 8.1, p201

¹³⁶ Whether or not the benefits in question amount to special commercial or financial advantage depends on the nature and extent of the obligations and their duration. Above, n.124 at para 43, p7

¹³⁷ Recital 14 of Regulation 1984/83

¹³⁸ Article 6(1) Regulation 1984/83

¹³⁹ Above, n.88 at p96 and above, n.90 at p479

¹⁴⁰ Recital 15 of Regulation 1984/83

was considered to promote a ‘dual co-operation’ between the parties, whilst, permitting long-term planning of sales and cost-effective production and distribution.¹⁴¹ However, the actual reality of being party to such a beer tie agreement may have been somewhat different with tenants long claiming of losses, not quantitative advantages, arising from their beer agreements.¹⁴²

Article 6 of Regulation 1984/83, permitted publicans to enter into an exclusive purchasing obligation with a brewery in respect of beer, and a drinks wholesaler in respect of a different type of beer and, or, other types of drinks.¹⁴³ However, in an attempt to limit the extent of the tie, which had come under criticism, especially in the UK, beer and drinks had to be specified by brand or denomination in the agreement.¹⁴⁴ Further, they had to be for resale in the premises used for the sale and consumption of drinks designated in the agreement, thereby limiting the tie to those premises. However, Article 6(2), stated that the Article 6(1) exemption would still apply where the exclusive purchasing obligations were imposed on the reseller in favour of the supplier by another undertaking which itself was not a supplier. Green notes this could cover several situations including where a wholesaler contracts with a dealer on the main supplier’s behalf.¹⁴⁵ Nevertheless, Korah and Rothnie rightly state that this is difficult to reconcile with the terms of the Guidelines and Recitals, which justified the tie on the basis of the advantages conferred by the supplier, itself, on the reseller.¹⁴⁶ The terms of Article 6(2) had no equivalent in Title III regarding petrol supply agreements.

2.2.3.4 The ‘white’ list for beer supply agreements

As stated above, in keeping with the prescriptive format established by Regulation 67/67, Title II of Regulation 1984/83 detailed exhaustive white lists of the permissible restrictions suppliers could impose on resellers. Article 7 detailed those in respect of beer supply agreements. However, Article 9 imported the terms of Articles 2(1) and 2(3) from Title I into Title II thereby permitting additional obligations to be imposed under beer supply agreements, such as requiring the reseller to purchase complete ranges of goods and minimum quantities of the contract goods. Article 7(1)(a) detailed the first ‘white’

¹⁴¹ Ibid

¹⁴² See above, n.62 at 291 citing Mrs Hand, Scottish Licence Trade Consultants, European Commission Public Hearing on Green Paper on Vertical Restraints, Brussels, October 6-7, 1997. Concerns of publicans were also recorded by the MMC in 1989. The Monopolies and Mergers Commission, *The Supply of Beer A Report on the supply of beer for retail sale in the United Kingdom* (Cm651, 1989) at Chapter 9 ‘Views of national victuallers’ associations and licensed tenants’

¹⁴³ Above, n.124 at para 44, p8

¹⁴⁴ Ibid at para 40, p7

¹⁴⁵ Above, n.90 at p450

¹⁴⁶ Above, n.16 at para 8.6, p210

obligation the supplier could impose on the reseller. This provided that the reseller could be obliged ‘not to sell beers and other drinks supplied by other undertakings which are of the same type as the beers or other drinks supplied under the agreement, in the designated premises.’ The Commission clarified that the obligation only applied where the supplier could meet the reseller’s demands.¹⁴⁷ Article 7(1)(b) then dealt with the situation where the reseller sold beers supplied by other undertakings which were a different type from those supplied under the agreement, and allowed the supplier to require that they only be sold in the designated premises in bottles or other small packages, unless their sale in draught form had been tolerated previously or was necessary to satisfy a sufficient demand from consumers. Consequently specialty beers could be sold but only in a form which did not directly compete with the principal supplier’s beer.¹⁴⁸ Under the terms of Article 7(1)(c) the supplier was permitted to impose restrictions on advertising competing products,¹⁴⁹ often causing them to be relegated to the back counter.¹⁵⁰

2.2.3.5 The ‘black’ list for beer supply agreement

As stated above, in keeping with Regulation 67/67’s approach Title II contained a ‘black’ list of restraints, the inclusion of which would deny an agreement the benefit of exemption. These limitations sought to restrict the extent and duration of the exclusive purchasing obligations imposed on resellers. Article 8(1)(a) stated that the reseller could not be expected to undertake an exclusive purchasing obligation in respect of goods or services not directly connected with the supply of drinks. Article 8(1)(b) prohibited any restriction on the reseller regarding the choice of supplier for goods or services which were not subject to an exclusive purchasing obligation or a ban on dealing in competing products. This blacklist clause affected the practice of UK brewers issuing tenants with a shortlist of suppliers of amusement machines who would give a share of their takings to the landlord.¹⁵¹ However, the Commission clarified that the installation of amusement machines in tenanted public houses could require the owner’s permission, which may be refused where it would impair the character of the premises; or the tenant could be restricted in the type of machine installed.¹⁵² Subsequently, in *re the Tenancy Agreement of*

¹⁴⁷ Above, n.124 at para 47, p8

¹⁴⁸ Above, n.90 at p481

¹⁴⁹ It could be required that this only be in proportion to the share of these goods in the total turnover realised in the premises. See Article 7(1)(c) Regulation 1984/83

¹⁵⁰ Above, n.90 at p481

¹⁵¹ Above, n.16 at para 8.19, p225

¹⁵² However, the Guidelines suggest that it was permissible for the owner of the public house to select such companies on the basis of “*objective criteria of a qualitative nature that are the same for all potential providers of such equipment and are applied in a non-discriminatory manner.*” Above, n.124 at para 52, p9

*Bass*¹⁵³ the Commission stated that it considered that the Bass policy at that time was compatible with the provisions of Regulation 1984/83.¹⁵⁴ Bass had to consent to the installation of amusement machines in its public houses and required a share of the takings of those machines. It had established a list of objective qualitative criteria to be met by the suppliers of the machines, and would consider whether suppliers suggested by the tenant qualified.¹⁵⁵

The Title II 'black' list was also concerned with the duration of the beer supply agreements. Articles 8(1)(c) and (d) reflected the Commission's concerns regarding foreclosure, and detailed the permitted periods for agreements. Whilst the permitted duration was affected by the extent of the tie it imposed on the reseller, this could not be indefinite in any case. Where the agreement concerned beer alone the maximum permitted duration of the agreement was ten years; and where drinks other than beer were also included, this was reduced to five years.¹⁵⁶ The Commission has indicated that the extended ten-year limit on beer supply agreements, with the same time frame applying to petrol station agreements, was due to the fact that resellers would generally be unable to repay the loans made to them by the other party to the agreement within five years.¹⁵⁷ Consequently the Commission maintained that the extended duration was influenced by practical considerations.¹⁵⁸ Article 8(1)(e) also denied exemption where the reseller was required to impose the exclusive purchasing obligation on his successors in title for a longer period than he himself would have been tied to the supplier, thereby preventing outlets being foreclosed for longer than the permitted duration.

However, notwithstanding the provisions of Article 8(1), Article 8(2)(a) provided that where premises are let to the reseller by the supplier, as under a tied tenancy, then the exclusive purchasing obligation could be imposed for the duration of the lease, even if this exceeded ten years, and could be renewed. The Commission sought to justify this as beer and petrol supply agreements require a substantial financial commitment by the supplier

¹⁵³ European Commission, *Notice pursuant to Article 19(3) of Regulation No 17 concerning notification No IV/32.491 – Bass Standard Tenancy agreement* ((1988) OJ C 285/5)

¹⁵⁴ *Ibid* at para 13, 7. The Commission clarified that this was compatible with the provisions of Regulation 1984/83 as explained by paragraph 52 of the Commission's Notice on the application of Article 85(3) of the Treaty to categories of exclusive distribution and exclusive purchasing agreements (1984) OJ C101/2

¹⁵⁵ Above, n.153 at para 13, 7. Also above, n.16 at para 8.19, p226. Further, in *Cutsforth and Others v. Mansfield Inns* [1986] 1 CMLR 1, the English High Court endorsed the approach laid out in the European Commission's Guidelines at paragraph 52. (*Cutsforth and Others* at paras 30-31, p9-10). While it was considered that a serious point of law had been raised the case settled out of court. (*Cutsforth and Others* at para 32, p10) Above, n.16 at para 8.19, p226-227

¹⁵⁶ See Article 5(1) (c) and (d). Also above, n.91 at p55

¹⁵⁷ Written Question No 2362/82 ([1983] OJ C279/1) at answer 3(a), p3. Also above, n.16 at para 8.20, p228

¹⁵⁸ Written Question No. 2362/82 ([1983] OJ C279/1) at answer 3(a), p3

justifying a lengthier obligation than in other sectors.¹⁵⁹ This was despite the fact that the Commission had acknowledged that networks of such agreements between drinks suppliers and resellers could potentially ‘immobilise competitive structures within national markets’ whilst also sealing them, with this being more likely where agreements are of longer duration and covered a range of products.¹⁶⁰ Consequently, this approach was contrary to that adopted in all other sectors, except petrol. However, in a bid to open up the market for other drinks,¹⁶¹ Article 8(2)(b) required the inclusion of a clause in the agreement, referred to as an ‘English Clause’. Where the public house was provided by the supplier, this clause permitted the reseller to acquire supplies of drinks, other than beer, from another source if they could be obtained more cheaply than from the supplier.¹⁶² However, the supplier had the opportunity to match the new offer. Article 8(2)(b)’s requirement to include an English Clause in the agreement was difficult to reconcile with Article 9 which incorporated Article 2(3) into Title II.¹⁶³ As Korah and Rothnie highlight, given the possibility for the supplier to require the reseller purchase minimum quantities of the contract goods, the reseller may struggle to afford to purchase much from outsiders, even if a substantial discount was offered.¹⁶⁴ This provision also controversially required the tenant inform the landlord of discounts offered by his competitors, with the Commission requiring that he do so ‘without delay’ so that the landlord has an opportunity to match such an offer.¹⁶⁵ In *Bass*, discussed above, the Commission accepted one week’s notice to allow the landlord to match any better offer made to the tenant.¹⁶⁶ This reduced the likelihood of the tenant obtaining supplies elsewhere on more favourable terms.¹⁶⁷ This was despite the fact, highlighted by Korah and Rothnie, that the anti-competitive implications of such clauses had been acknowledged in other sectors, as in *BP Kemi*.¹⁶⁸ There the Commission noted that such clauses could be used as a mechanism for the exchange of information regarding prices and conditions between competitors.¹⁶⁹

¹⁵⁹ Above, n.112 at para 30, p37

¹⁶⁰ Above, n.158 at answer 2(a) and (b), p2

¹⁶¹ See Recital 18 Regulation 1984/83

¹⁶² Article 8(2)(b). Above, n.91 at p56.

¹⁶³ Above, n.16 at para 8.21, p229

¹⁶⁴ Ibid at para 8.21, p229-230

¹⁶⁵ Above, n.124 at para 55, p9

¹⁶⁶ Above, n.153 at para 9, p6

¹⁶⁷ Above, n.16 at para 8.21, p230

¹⁶⁸ Commission Decision of 5 September 1979 in Case IV/29.021 *BP Kemi- DDSF* ([1979] OJ L286/32)

¹⁶⁹ Ibid at para 64, p42. Also J Goyder, *EU Distribution Law* 5th Edition (Oxford, Hart Publishing, 2011) at para 3.3.8.3, p94

2.2.4 UK reaction to the new rules

However, Title II received a mixed response from brewers and publicans. As Green highlights by limiting the exemption to purchasing agreements for the supply of beer alone, breweries claimed that the loss of revenue caused by cutting the tie on wines and spirits would necessitate an increase in beer prices and rents to compensate them.¹⁷⁰ Brewers also argued that loss of control over the drinks sold in their pubs would damage their reputation and the resulting shift in the balance between tenancy and management would cause more pubs to be changed to company managed rather than tenanted outlets on the expiration of existing leases.¹⁷¹ However, as Green notes, there was no evidence that these consequences were economically necessary.¹⁷² By contrast, some publicans welcomed the reforms as having the potential to loosen the Brewers' economic hold over them and introducing the possibility of purchasing wines and spirits from other sources at competitive prices.¹⁷³ There was, however, skepticism over this. Sinan rightly regards the Regulation as “*a victory for the Brewers' lobby*” as they would face little difficulty drafting their agreements to fulfill the Regulation's requirements. It was also unlikely that in the event of a brewer's agreement failing to comply strictly with the terms of Regulation 1984/83 that individual notifications would have a meaningful impact on the relationship between the publicans and their brewers. This was due to the fact there would always be the option to modify the notified agreements, thereby ensuring compliance.¹⁷⁴

2.2.5 The European Commission's on-going approval of tying agreements

Following the adoption of Regulation 1984/83, the Commission approved beer supply agreements under the Regulation, as well as on an individual exception basis. This practice was exemplified in *Carlsberg*¹⁷⁵ in 1984. There, Metropolitan was granted exclusive rights to produce, market and sell Carlsberg beer in the UK in return for royalty payments. The agreement was granted an exemption under Article 101(3) TFEU on satisfaction of its efficiency enhancing criteria, discussed above. The Commission referenced the peculiarities of the British beer market with most outlets being foreclosed, making it unlikely that Carlsberg could penetrate this as efficiently and so enhance competition in the

¹⁷⁰ N Green, 'New EEC Legislation on Exclusive Dealing and Purchasing – III: Exclusive Purchasing' (1983) 133 New L.J. 693 at 694

¹⁷¹ Ibid at 694

¹⁷² Ibid at 694

¹⁷³ Ibid at 694 -695

¹⁷⁴ Above, n.104 at 1065

¹⁷⁵ Commission Decision of 12 July 1984 in Case IV/30.129 *Carlsberg* ([1984] OJ L207/26)

market, without the agreement granting access to Metropolitan's tied houses.¹⁷⁶ Consequently, the agreement which was to be operated for eleven years was exempted on the basis of the peculiar structure of the UK beer market which made it necessary for foreign brewers wishing to enter the market to obtain the assistance of a national brewer.¹⁷⁷ This contrasted with the Commission's decision in *Re Soda ash*¹⁷⁸ where the parties were involved in the chemical industry, and their five-year agreement incorporating an exclusive purchasing obligation had to be reduced to a two-year non-exclusive agreement.¹⁷⁹ However, in 1989, the Commission announced its intention to approve another agreement similar to that in *Carlsberg*, involving Moosehead Breweries of Canada and Whitbread.¹⁸⁰ The agreement was for an indefinite duration and granted Whitbread the exclusive right to produce, market and sell Moosehead in return for a royalty payment.¹⁸¹ Again, in doing so, the Commission highlighted the distinguishing features of the British beer market¹⁸² with this being a determining factor in its decision, as foreign brewers' required the assistance of a large national brewery to access the UK market.¹⁸³

At this time the Commission also began to approve the terms of standard form tenancy agreements submitted by brewers, such as *Bass*.¹⁸⁴ In considering Bass's notified agreement, the Commission noted the concentrated nature of the UK market and that a larger proportion of on-licensed premises in the UK were owned and operated by brewers than in any other Member State.¹⁸⁵ The notified standard tenancy agreement incorporated a standard tying clause and was considered to comply with Regulation 1984/83.¹⁸⁶ However, possibly influenced by the prevailing competitive conditions in the UK market at that time, the Commission stated that the exemption was only granted for a period of five years.¹⁸⁷ Nevertheless, as Everreste notes, this tolerance of beer agreements contrasted with the

¹⁷⁶ Ibid at p30-31 and para 8, p34

¹⁷⁷ Exception was granted until 30 September 1991. This was considered a sufficient period for Carlsberg to establish its own sales network and become independent of other large breweries for the distribution of its products. Above, n.175 at p30-31 and para 8, p34. Also above, n.121 at 609

¹⁷⁸ Commission of the European Communities, *Eleventh Report on Competition Policy* (Brussels, 1982) at para 73, p53

¹⁷⁹ The agreement did involve Solvay and ICI who were the largest producers of soda ash at that time. Ibid at para 73-76, p53-54

¹⁸⁰ European Commission, *Notice pursuant to Article 19(3) of Council Regulation No 17 concerning notification No IV/32.736 – Moosehead/ Whitbread* ((1989) OJ C179/13)

¹⁸¹ Ibid at para 7.2, 13 and para 11, 14

¹⁸² These included the fact that most beer in the UK was sold in draught form in public houses; 81% of all beer in the UK was sold via on-trade premises; and to achieve any significant sales volume, access to a certain number of public houses was required. They also referenced the high number of tied houses in the UK market, making it 'indispensible' for an overseas brewer to be assisted by a national brewer to enter the UK market. Above, n.180 at para 6.2 and para 6.4, p13

¹⁸³ Ibid at para 6.4, p13

¹⁸⁴ Above, n.153

¹⁸⁵ Ibid at para 4(b) and para 4(c), p5

¹⁸⁶ Ibid at para 7, p6 and para 9, p6 and p8

¹⁸⁷ Ibid at p8

approach adopted to similar agreements in other sectors, with very few such exemptions being granted.¹⁸⁸ This was exemplified by the Commission's decision in *Spices*.¹⁸⁹ The Commission found an exclusive purchasing agreement between spice producer Liebig, which accounted for 39% of the Belgian market, and the three largest supermarket chains, did not qualify for exemption under Regulation 67/67 then in force, or for individual exemption under Article 101(3) TFEU.¹⁹⁰ The agreement was largely identical in its essential aspects to a brewery tying agreement, requiring the supermarkets to sell only Liebig spices and their own brand spices. However, in considering the agreement, the Commission held that whilst it was beneficial to the parties to the agreement, consumers did not share in the benefits as their choices were restricted and prices increased.¹⁹¹ Consequently it violated the terms of Article 101(1) TFEU. However, given the significant similarities between the essential terms of the agreement in the *Spices* decision and those of a beer tying agreement, Everreste correctly suggests that the *Spices* Decision highlights the European Commission's 'special deference' towards breweries.¹⁹² Everreste also suggests that this policy on brewery agreements was influenced by the "*entrenched and long-established*" tied house system across most of the EU.¹⁹³ This was supported by the Commission's estimate that there was approximately a quarter of a million tied house agreements in existence in the EU in 1983.¹⁹⁴ Agreements of this type were therefore of significant economic importance and so most likely influenced the Commission's decision making at that time. As already discussed in Chapter 2, the strength of the lobbying in the brewers' corner was also evident in the UK's failure to implement the Monopolies and Mergers Commission's (MMC) original proposals in its 1989 report, instead implementing weaker versions of these through the Beer Orders in 1989.¹⁹⁵

2.2.6 The EU's 1990 Beer Review

Although the Beer Orders as ultimately implemented in the UK in 1989 were a weakened version of the MMC's original proposals, the terms of the MMC's 1989 Report¹⁹⁶ were sufficiently controversial to prompt the Vice President of the European Commission, in

¹⁸⁸ Above, n.121 at 609-610

¹⁸⁹ Commission Decision of 21 December 1977 in Case IV/29.418 *Spices* ([1978] OJ L53/20)

¹⁹⁰ Ibid at para 25 and para 26, p25

¹⁹¹ Ibid at para 26, p25

¹⁹² Above, n.121 at 610

¹⁹³ Ibid at 610

¹⁹⁴ Above, n.110 at answer at para 1(a), p23

¹⁹⁵ Chapter 2, p35-36

¹⁹⁶ See Chapter 2

March 1989, to commission a review of the EU beer market.¹⁹⁷ The announcement of the review was simultaneous with the publication of the MMC's Report. However, the 'official' justification provided for the review was to determine whether there were any significant competitive obstacles obstructing the opening of national markets in the lead up to the creation of the single market in 1992, and whether additional measures were required to achieve this.¹⁹⁸ Given the Commission and the Court's decisional practices in the years immediately preceding this review, noted above, an adverse outcome was not expected, and was not delivered.¹⁹⁹ It was found that countries that operated tied-house systems, including the UK, enjoyed a "*proliferation of small and medium-sized breweries*" and offered their consumers the greatest choice of brands.²⁰⁰ This contrasted with countries with "*open*" systems, such as the USA and Australia,²⁰¹ where one or two large breweries tended to dominate and benefitted from significant economies of scale.²⁰² Within Europe, the Commission found that the tied house system only existed in the "*developed and static North European markets*" with this being most prevalent in the UK.²⁰³ Consequently, one of the Commission's primary conclusions following its review was that no general changes were required to EU rules governing beer agreements. However, the Commission would consider whether further measures were required in the UK once the Beer Orders had taken effect.²⁰⁴ It highlighted that 62% of beer sales passed through the UK's tied houses, with the situation being worsened by the restrictive licensing system in operation, which restricted the number of new retailers entering the UK market.²⁰⁵ Given the lack of proposals at that time to amend the restrictive licensing regime in the UK, Maitland-Walker correctly asserts that the Commission was simply waiting to establish the impact the Beer Orders have on the UK market.²⁰⁶ As Maitland-Walker also asserts, this approach suggested an implicit approval of the Beer Orders thereby making it unlikely that the

¹⁹⁷ Commission of the European Communities, *XXth Report on Competition Policy* (1990, Brussels) at p68-70.

¹⁹⁸ Ibid at para 85, p68. See also J Maitland-Walker, 'Editorial, The EEC review: much ado about nothing' (1990) 11(4) E.C.L.Rev 131

¹⁹⁹ Above, n.197. Also Press Release, 'Sir Leon Brittan Announces the Results of the EEC Beer Review' (14th June 1990) Brussels IP/90/470 (*Europa*)

<<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/90/472&format=HTML&aged=1&language=EN&guiLanguage=en>> accessed 13th July 2011

²⁰⁰ Press Release, 'Sir Leon Brittan Announces the Results of the EEC Beer Review' (14th June 1990) Brussels IP/90/470 (*Europa*)

<<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/90/472&format=HTML&aged=1&language=EN&guiLanguage=en>> accessed 13th July 2011

²⁰¹ See Chapter 5

²⁰² Above, n.200 at p4

²⁰³ Ibid at p5

²⁰⁴ Ibid at p1

²⁰⁵ Ibid at p5

²⁰⁶ J Maitland-Walker, 'Editorial, The EEC review: much ado about nothing' (1990) 11(4) E.C.L.Rev 131 at 132

Commission would seek to challenge these on the grounds of incompatibility with EU law.²⁰⁷

However, in addition to the consideration of the tied house system and the peculiarities of the UK beer market, the review considered the matter of exclusive purchasing agreements concluded by small breweries and the application of the *de minimis* rule to these.²⁰⁸ In contrast to the agreements of large breweries, the Commission concluded that the exclusive purchasing agreements of small regional brewers should be governed by national law not the EU competition law provisions.²⁰⁹ The Commission's consideration of these arrangements was prompted by confusion at that time amongst small brewers as to whether the EU competition law provisions were applicable to their tying agreements. This confusion had resulted in litigation between such small brewers and their resellers over the legality of their exclusive purchasing agreements.²¹⁰ The decision that these should be governed by national law was reached on the assumption that the risk of market foreclosure was effectively managed by confining the restrictions imposed on tying agreements to the largest brewers who accounted for the greatest proportion of beer sales.²¹¹ Such agreements of small brewers would not normally restrict competition or affect trade to an appreciable extent as required by Article 101(1) TFEU. However, the Commission stated that it believed this to be the correct position even where other parallel agreements concluded by other brewers existed.²¹² This conclusion was noted to be without prejudice to the CJEU's judgment in *Delimitis v Henninger Bräu*,²¹³ although as will be discussed below, there is difficulty in reconciling the two positions.²¹⁴

²⁰⁷ Ibid at 133

²⁰⁸ As noted at para 1.2.3 above, this principle has its roots in the EU goal of protecting SMEs.

²⁰⁹ Above, n.200 at p1

²¹⁰ Ibid at p3

²¹¹ Ibid at p3

²¹² Ibid at p3

²¹³ At the time of the review, the EU was determining at what level the *de minimis* principle should apply to brewery contracts with a notice later being produced on this. The review also considered the licensing agreements between major brewers, such as Carlsberg and Metropolitan, discussed above. It concluded that these agreements should be examined to determine whether they were being used to divide the market or control imports. Above, n.200 at p1 and p3.

²¹⁴ Above, n.206 at 134 where the author also makes this argument

2.2.7 The CJEU's approach in *Delimitis*

The CJEU was required for the first time in *Delimitis v. Henninger Bräu*,²¹⁵ to interpret the application of Regulation 1984/83 to beer supply agreements. In doing so it demonstrated a less mechanistic approach to the application of the competition provisions than had long been demonstrated by the Commission, as noted above.²¹⁶ The CJEU took the opportunity to clarify the status of those agreements whilst also ruling on several important matters, thereby refining its decision in *De Haecht*.²¹⁷ It laid down two cumulative conditions which had to be satisfied before a beer supply agreement would be found to come within Article 101(1) TFEU, with foreclosure effect being a determining factor.²¹⁸

By way of a preliminary reference, the CJEU was required to answer several questions regarding the interpretation of certain provisions in Regulation 1984/83. Specific requirements of Regulation 1984/83 appeared not to be satisfied by the terms of *Delimitis*'s beer supply agreement. The primary problem was that the drinks affected by the purchasing obligation were not specified in the contract but in the brewer's price list, which would be amended 'from time to time'; and the agreement did not include an 'English clause' regarding drinks other than beer.²¹⁹ The CJEU clarified that Regulation 1984/83 required that the agreement itself contain a list of the drinks affected, it not being sufficient to refer to the brewer's price list; and the necessary 'English clause' had to be included for exemption to be possible.²²⁰ As the beer supply agreement did not qualify from exemption under Regulation 1984/83, the CJEU had to consider whether the agreement came within Article 101 TFEU. In doing so, focus was placed on the foreclosure effects of such beer supply agreements.

Building on its decision in *de Haecht*, the CJEU held that the object of beer supply agreements was not to restrict competition, referring instead to the benefits flowing from

²¹⁵ (Case C-234/89) *Stergios Delimitis v Henninger Bräu AG* [1991] ECR I-935; [1992] 5 CMLR 210. The CJEU referred to a beer supply agreement as an agreement where "*the supplier generally affords the reseller certain economic and financial benefits... In consideration for those benefits, the reseller normally undertakes, for a predetermined period, to obtain supplies of the products covered by the contract only from the supplier.*" ([1992] 5 CMLR 210 at para 10, p244-245)

²¹⁶ Above, n.9 at 284-285. Korah also notes the Commission's long history of decisions treating any important restriction on conduct as anti-competitive. V Korah, 'The judgment in *Delimitis*: a milestone towards a realistic assessment of the effects of an agreement or a damp squib?' (1992) 14(5) E.I.P.R 167 at 176

²¹⁷ Above, n.93

²¹⁸ (Case C-234/89) *Stergios Delimitis v Henninger Bräu AG* [1992] 5 CMLR 210 at p212. This concerned a beer supply agreement for a cafe in Germany. *Delimitis* sued the owning brewery to which the café was tied and claimed the agreement was, inter alia, void under Article 101(1) TFEU. The German court initially held that the agreement did not affect trade between Member States, however, on appeal the matter was referred to the CJEU for a preliminary ruling ([1992] 5 CMLR 210 at 216-219).

²¹⁹ *Ibid* at p244

²²⁰ *Ibid* at para 37-39, p250

such agreements.²²¹ However, even although beer supply agreements did not have the object of restricting competition, the CJEU stated that it was necessary to ascertain whether the agreement had that effect.²²² In doing so, the Court referenced its judgment in *de Haecht* and emphasised the need to examine the effects of such an agreement on the market in the specific context in which they occurred,²²³ and where they may combine with other such agreements to have a cumulative effect on competition.²²⁴ The relevant product and geographical market therefore had to be determined. The CJEU stated:

“[b]eer is sold through both retail channels and premises for the sale and consumption of drinks. From the customer’s point of view, the latter sector, comprising in particular public houses and restaurants, may be distinguished from the retail sector on the grounds that the sale of beer in public houses does not solely consist of the purchase of a product but is also linked to the provision of services... The specific nature of the public house trade is borne out by the fact that breweries organise specific distribution systems for this sector which require special installations, and that the prices charged in that sector are generally higher than retail prices.

*It follows that in the present case the reference market is that for the distribution of beer in premises for the sale and consumption of drinks.”*²²⁵

The CJEU also noted that most supply agreements were entered into at the national level and so account was to be taken of the UK market for beer distribution in premises for the sale and consumption of drinks.²²⁶ Having determined the relevant market, the CJEU established two cumulative conditions that had to be satisfied in order for a beer supply agreement to be prohibited under Article 101(1) TFEU. In doing so, it further refined its *de Haecht* decision.²²⁷ The first condition laid down by the Court was that having regard to the ‘economic and legal context of the agreement it must be difficult for new entrants to increase their market share to gain access to the domestic market for the distribution of beer in premises for the sale and consumption of drinks’.²²⁸ Consequently, the agreement must be one of a number of similar agreements on the market that have a cumulative foreclosing effect on competition. However that in itself was only one factor in

²²¹ Ibid at para 10-13, p244-245

²²² Ibid at para 13, p245

²²³ Above, n.12 at p578

²²⁴ Above, n.218 at para 14, p245. See also V Korah, ‘The judgment in Delimits: a milestone towards a realistic assessment of the effects of an agreement or a damp squib?’ (1992) 14(5) E.I.P.R 167 at 171

²²⁵ Above, n.218 at para 16-17, p245-246

²²⁶ Ibid at 211

²²⁷ Ibid at para 27, p248. Also S.E. Wheeler and J. Shaw, ‘Case Comment Networks of Similar Agreements’ (1991) 16(6) E.L.Rev 520 at 520

²²⁸ Above, n.218 at para 27, p248

determining whether access to the market is difficult.²²⁹ Secondly, the CJEU required that ‘the agreement in dispute must make a significant contribution to the cumulative effect produced by all those agreements in their legal and economic context’.²³⁰ It highlighted that beer supply agreements entered into by brewers who only make an insignificant contribution to the cumulative effect of such agreements, are outwith the Article 101(1) TFEU prohibition.²³¹ Consequently the CJEU’s position appears to conflict with the Commission’s in the 1990 Beer Review, noted above, that agreements of small brewers would not normally restrict competition or affect trade to an appreciable extent *even* where other parallel agreements concluded by other brewers existed.²³² The CJEU’s ruling clarified that such agreements can be caught by as Article 101(1) TFEU where the agreement is one of several similar agreements which have the combined effect of distorting competition in the marketplace.²³³

Wheeler and Shaw also suggest that the CJEU’s assertion that beer supply agreements entered into by brewers who only make an insignificant contribution to the cumulative effect of such agreements, are out with the Article 101(1) TFEU prohibition was an indication that the Court was hinting at a role for the *de minimis* doctrine.²³⁴ However, in determining the contribution made by an individual agreement, the CJEU highlighted not only the importance of the contracting parties market position in the relevant market but also the duration of the agreement.²³⁵ Long-term contracts were more likely to restrict competition than short-term ones, even where the brewer had a small market share.²³⁶ This position was potentially at odds with Wheeler and Shaw’s assertion. The CJEU clarified that even a brewer with a relatively small market share, which ties its sales outlets for several years, contributes significantly to the sealing off of the market in the same way as a brewer with a significant market position which regularly releases those outlets at shorter intervals.²³⁷ Consequently all beer supply agreements, including those of small brewers, had to be assessed according to the two cumulative conditions established by the CJEU.²³⁸ Further, in adopting this two-stage approach, the CJEU’s judgment could potentially be

²²⁹ Ibid at para 27, p248

²³⁰ Ibid at para 27, p248

²³¹ Ibid at para 24, p247

²³² Above, n.200 at p3

²³³ Above, n.206 at 134

²³⁴ Above, n.218 at para 24, p248 and ‘Case Comment Networks of Similar Agreements’ (1991) 16(6) E.L.Rev 520 at 523-524

²³⁵ Above, n.218 at para 24, p248

²³⁶ Ibid at para 26, p248

²³⁷ Ibid at para 26, p248

²³⁸ As this was a preliminary reference, no conclusions were reached on the facts of the case

applied to exclusive purchasing obligations in other sectors of the economy.²³⁹ Korah considers the judgment to be “*an important milestone along the road to a more realistic attitude being taken towards assessing the effects of all kinds of agreements on competition.*”²⁴⁰

2.2.8 Post *Delimitis*

In 1992, shortly after the CJEU’s decision in *Delimitis*, the Commission undertook to clarify the application of the *de-minimis* principle to agreements of small brewers.²⁴¹ It had touched upon this in its EU Beer Review discussed above but provided little guidance. It issued Notes of Guidance²⁴² amending the existing notice on Regulation 1983/83 and 1984/83.²⁴³ Guideline 40 clarified that beer agreements were generally excluded from Article 101(1) TFEU where the brewery had a national market share of less than 1% and did not produce more than 200,000 hectolitres of beer per annum.²⁴⁴ However, reflecting the CJEU’s foreclosure concerns in *Delimitis*, the *de minimis* provision was only applicable where the agreement was for no more than 7.5 years where it covered beer and other drinks; and no more than 15 years, where it covered only beer.²⁴⁵ As Weston and Pheasant note, the 1% threshold for brewers was significantly lower than the 5% for undertakings in other sectors, thereby potentially recognising the foreclosure risk within this market due to the extensive use of exclusive purchasing agreements.²⁴⁶ However, the Commission did also indicate that even where the *de minimis* conditions outlined in the notice are not satisfied, there was still a possibility Article 101(1) TFEU would not be applicable. This was where the number of outlets tied to the undertakings party to the agreement was limited compared to the number of outlets existing in the market, as such an agreement may still have a negligible effect on trade between Member States or

²³⁹ The CJEU’s decision was upheld in (T-7/93) *Langnese-Iglo v. E.C. Commission* [1995] ECR II-1533

²⁴⁰ V Korah, ‘The judgment in *Delimitis*: a milestone towards a realistic assessment of the effects of an agreement or a damp squib?’ (1992) 14(5) E.I.P.R. 167 at p176

²⁴¹ Above, n.206 at 134

²⁴² European Commission, *Notice modifying the notice concerning Commission Regulations (EEC) No 1983/83 and (EEC) No 1984/83 of 22 June 1983 on the application of Article 85 (3) of the EEC Treaty to categories of exclusive distribution and exclusive purchasing agreements* ((1992) OJ C121/2). J Ratliff, ‘Major themes of EEC Competition law in 1992’ (1993) 4(2) I.C.C.L.R. 56 at 60

²⁴³ Above, n.124

²⁴⁴ European Commission, *Notice modifying the notice concerning Commission Regulations (EEC) No 1983/83 and (EEC) No 1984/83 of 22 June 1983 on the application of Article 85 (3) of the EEC Treaty to categories of exclusive distribution and exclusive purchasing agreements* ((1992) OJ C121/2)

²⁴⁵ The Notice also clarified that these principles were applicable to beer supply agreements concluded by wholesalers, taking into account the position of the brewery whose beer is the primary subject of the agreement

²⁴⁶ D Weston and J Pheasant, ‘Vertical Restraints, Foreclosure and Article 85 Developing an analytical framework’ (1997) 18(5) E.C.L.Rev. 323 at 326

competition.²⁴⁷ It was further clarified that these changes were without prejudice to the application of national law to the agreements covered by it. The Notice was therefore without prejudice to the application of the Beer Orders in the UK, discussed in Chapter 2.

The Commission's newly clarified position on the application of the *de minimis* principle to beer supply agreements came into play when Mr and Mrs Roberts, the tenants of Greene King, a small UK regional brewer and pubco, alleged that the beer purchasing obligation in their beer supply agreement infringed Article 101(1) TFEU.²⁴⁸ They claimed the tying provision in their lease was incompatible with the treaty provision. In considering their application, the Commission established that as the hectoliter and duration thresholds of the beer *de minimis* Notice were not satisfied, Greene King could not benefit from it.²⁴⁹ It applied the CJEU's judgment in *Delimitis* to the agreement. Greene King was not considered to have sufficient market power to contribute significantly to the market foreclosure. Its total tied network only accounted for 1.3% of volume beer through put in the UK on-trade market by comparison to the 5%, or more, market shares held by the largest brewers at that time.²⁵⁰ Also, the agreement's nine-year duration was significantly less than the twenty-year or longer duration of other operators.²⁵¹ The Commission subsequently concluded that the agreement did not fall within the scope of Article 101(1) TFEU. Mr and Mrs Roberts appealed the Commission's decision however it was upheld by the General Court.²⁵²

The Court held that the definition of the relevant market was as stated by the CJEU in *Delimitis*, being 'establishments selling alcoholic beverages for consumption on the premises and not public houses alone'.²⁵³ The Commission was considered to have correctly assessed the effects of Green King's network of agreements noting that their market share was very small and the duration of their agreements was not "*manifestly excessive*".²⁵⁴ The Commission was also correct to reject the argument that Greene King's network of 'downstream' agreements could be attributed to the supplying breweries, which

²⁴⁷ Above, n.244

²⁴⁸ Commission Decision of 12 November 1998 in Case IV/36.511/F3-Roberts/ Greene King (*Europa*) <<http://ec.europa.eu/competition/antitrust/closed/en/iv36511.pdf>> accessed 9th February 2015. They owned approximately 1100 pubs and had loan tied with 1,500 other outlets. Also P Bridgeland, 'New case law on market foreclosure. Court of First Instance upholds three Commission decisions relating to beer ties' (2002) (2) ECCPN 45

²⁴⁹ Commission Decision of 12 November 1998 in Case IV/36.511/F3-Roberts/ Greene King at para 99, p22 (*Europa*) <<http://ec.europa.eu/competition/antitrust/closed/en/iv36511.pdf>> accessed 9th February 2015

²⁵⁰ Ibid at para 102, p23

²⁵¹ Ibid at para 102, p23

²⁵² (T25/99) *Roberts and Roberts v E.C. Commission* [2001] ECR II-1881; [2001] 5 CMLR 21.

²⁵³ (T25/99) *Roberts and Roberts v E.C. Commission* [2001] 5 CMLR 21 at H10, p830-831

²⁵⁴ Ibid at H10, p831

had concluded beer supply agreements with Greene King.²⁵⁵ Reliance was placed on the Commission's earlier decision in *Inntrepreneur and Spring*.²⁵⁶ For the supply agreements between the wholesaling brewery, such as Greene King, and the supplying breweries, namely the national brewers, ('upstream agreements') to form part of the supplying breweries' network of agreements, they had to contain a purchasing obligation.²⁵⁷ For these upstream agreements and those agreements concluded between the wholesaling brewers and their tied establishments ('downstream agreements') to be attributed to the supplying breweries' network of agreements, it was deemed necessary that the agreements between the supplying breweries and the wholesaling brewery be sufficiently restrictive that access to the wholesaling brewer's network of downstream agreements is very difficult or no longer possible for other brewers.²⁵⁸ If the restrictive effect of the upstream agreement is limited, then other brewers are free to enter supply agreements with the wholesaling brewer and so enter their network of downstream agreements, enabling them to have access to all premises within that network without having to conclude individual agreements with each outlet.²⁵⁹ This was considered to promote penetration of the market by other breweries.²⁶⁰ Consequently the assessment of downstream agreements had to be distinguished from the assessment of the upstream agreements.²⁶¹

Greene King's supply agreements with the national breweries were not very restrictive with the most restrictive agreements having only a minimum purchasing obligation of less than 20% of the beer it sells wholesale, so at least 80% of that beer may come from other brewers.²⁶² As a result those agreements were deemed to be so little restrictive "*that access to Greene King's network of "downstream" agreements was not seriously compromised for other breweries, even taking the cumulative effect of those agreements into account.*"²⁶³ Greene King was not precluded from sourcing from a number of brewers and the agreements failed to contribute significantly to the foreclosure of the market as required by *Delimitis*. In rejecting the appeal, the Court held that the Commission had correctly established that the agreement was out with the scope of Article 101(1) TFEU.²⁶⁴ Consequently, in light of the foregoing, the Commission, as upheld by the General Court,

²⁵⁵ Ibid at para 114, p852

²⁵⁶ Commission Decision of 29 June 2000 in Cases IV/36.456/F3 *Inntrepreneur* and IV/36.492/F3 *Spring* [2000] OJ L195/49

²⁵⁷ Above, n.253 at para 106, p850

²⁵⁸ Ibid at para 107, p850

²⁵⁹ Ibid at para 108, p850

²⁶⁰ Ibid at para 108, p850-851

²⁶¹ Ibid at para 109, p851

²⁶² Ibid at para 113, p851

²⁶³ Ibid at para 113, p851

²⁶⁴ Ibid at H10, p831. Also P Bridgeland, 'New case law on market foreclosure. Court of First Instance upholds three Commission decisions relating to beer ties' (2002) (2) ECCPN 45

appeared to follow the CJEU's approach in *Delimitis* by adopting a less mechanistic style in its handling of vertical restraints generally. The decision was also considered to be of importance in allowing the Commission to focus on the restrictive agreements of national brewers, rather than being tied up in the handling of agreements of small brewers.²⁶⁵

The Commission in its decision in *Inntrepreneur and Spring*, which was followed in *Roberts* with regard to distinguishing the assessment of upstream and downstream agreements, considered the notified leases of pubcos *Inntrepreneur* and *Spring*.²⁶⁶ The pubcos had extensive tied estates and imposed a comprehensive tying obligation on tenants which specified seventeen different types of beers, the brands and denominations of which were detailed in the company's price list to which the company could 'add, substitute or delete brands or denominations' as often as it wished.²⁶⁷ The Commission noted that in contrast to *Delimitis*, which was concerned with a brewer's agreements, here the notifying party was a pubco which was not vertically integrated with any brewer.²⁶⁸ It established that the relationship between pubcos and their tenants and its relationship with brewers was economically different from a brewer selling beer through its own network of agreements.²⁶⁹ The Commission highlighted the pubcos' practice of 'multi-sourcing' and 'periodic tendering,' and considered their portfolios to be diversified and included products of regional and national brewers.²⁷⁰ The duration of the contracts with supplying brewers was structured so that a proportion of business could be re-tendered frequently and the notifying pubcos did not have a volume commitment with any of the 18 brewers whose brands were listed on their price list.²⁷¹ It subsequently took a very favourable view of this arrangement and commented that this made the notifying parties 'gateways' for a large number of brewers and potentially for all national and foreign brewers.²⁷² It concluded that the tied leases of a non-tied pubco were more likely to enhance the competitive structure of the market than contribute to foreclosure.²⁷³ This was despite the fact, as discussed in Chapter 2, small brewers still struggled to penetrate the market at the retail level due to the practices of such pubcos. The focus on the effect of the pubcos' upstream agreements continued as the Commission relied on the perceived foregoing benefits to dismiss the importance of considering the situation at the retail level where significant concerns were

²⁶⁵ Press Release, 'The tied pub leases of small and regional UK brewers fall outside the reach of European competition rules' (6th November 1998) Brussels IP/98/967

²⁶⁶ Above, n.256 at para 55-56, p56

²⁶⁷ Ibid at para 36-37, p53

²⁶⁸ Ibid at para 59, p56

²⁶⁹ Ibid at para 59, p56

²⁷⁰ Ibid at para 60, p56

²⁷¹ Ibid at para 60, p56

²⁷² Ibid at para 60, p56

²⁷³ Ibid at para 62, p56

being expressed with regard to the UK beer market.²⁷⁴ In light of the pubcos' sourcing arrangements it stated that the "*importance of a pub company's tied estate (in terms of number of outlets tied and beer throughput of those outlets) is not currently relevant to an assessment of the contribution to market foreclosure.*"²⁷⁵ The pubcos were therefore deemed not to operate a network of 'restrictive' agreements that significantly contributed to the foreclosure of the UK on-trade beer market and their standard leases were also deemed not to form part of the supplying brewer's tied network.²⁷⁶ Given its focus on the upstream market, the Commission concluded that the exclusive purchasing agreements and non-compete obligations in the notified leases did not come within Article 101(1) TFEU.²⁷⁷

2.2.9 The Commission's continued approval of beer supply agreements

The Commission's deference towards beer supply agreements, discussed above, continued. In 1994 it published a Notice of its intention to grant retroactive individual exemption from Article 101(1) TFEU to the standard form 'Inntrepreneur' lease of Inntrepreneur Estates Limited (IEL), one of the UK's largest pubcos.²⁷⁸ The parties had sought either negative clearance or exemption under Regulation 1984/83.²⁷⁹ The Commission, without explaining the clauses that precluded exemption under Regulation 1984/83, rejected the parties' request in favour of the granting of individual exemption under Article 101(3) TFEU. It has been suggested that exemption was precluded as the tying provision of the lease referred to twelve generic types of beer, not brands, as required, and effectively included all beers sold in the UK.²⁸⁰ The Commission's Notice also failed to make clear the advantages bestowed on the tenant under the terms of the lease, it only being stated that Inntrepreneur expected the rent to be lower than that paid by free-of-tie tenants, but 'the terms were otherwise comparable in all respects'.²⁸¹ The publication of the Notice caused the Commission to receive numerous complaints from Inntrepreneur's tenants.²⁸² This prompted the Commission in February 1995 to request the Office of Fair Trading (OFT) to

²⁷⁴ Ibid at para 62, p56

²⁷⁵ Ibid at para 62, p56

²⁷⁶ Ibid at para 63, p57

²⁷⁷ Ibid at para 64, p57

²⁷⁸ See chapter 2. European Commission, *Notice published pursuant to Article 19(3) of Regulation 17 concerning notification* No IV/34.387–*Inntrepreneur-GM-Courage* (1993) OJ C206/2

²⁷⁹ European Commission, *Notice published pursuant to Article 19(3) of Regulation 17 concerning notification* No IV/34.387–*Inntrepreneur-GM-Courage* (1993) OJ C206/2 at para 1, p2

²⁸⁰ Ibid at para 9, p4 and 'Case Comment Inntrepreneur/ GM/ Courage' (1994) 15(1) E.C.L.Rev R6 at R6

²⁸¹ Above, n.279 at para 15, p5

²⁸² A MacCulloch, 'Case Comment Inntrepreneur Estates: Co-operative application of the EC competition rules in the United Kingdom?' (1995) 16(6) E.C.L.Rev 380 at 380

launch an inquiry into brewers' wholesale pricing policies.²⁸³ In doing so, the OFT referenced the Commission's concerns over Innpreneur tenants being forced to purchase beer from Courage at significantly inflated prices by comparison to free-of-tie customers, and that other large brewers pursued a similar strategy thereby placing lessees in a position where they were unable to compete.²⁸⁴ The terms of the report were not made public, however the OFT ultimately declared that tenants were charged fair wholesale prices and that pubcos had increased retail competition in the UK market.²⁸⁵ The Director General of Fair Trading, stated that "[w]hile the exact trade-off between the value of discounts on the price of beer and other benefits cannot be a subject for precision, I do not believe that price differentials have...operated to the detriment of the tied trade."²⁸⁶ It therefore followed the European position that the countervailing benefits of the tie justify it as a legitimate business model, despite the numerous concerns being raised over the operation of the UK beer tie at that time.

The Commission subsequently continued undeterred and granted retroactive exemption to the notified standard leases of the UK's three largest breweries Whitbread, Bass and Scottish & Newcastle.²⁸⁷ Two factors had prompted these brewers to notify their leases to the Commission. Firstly, the Commission did not consider that the beer tie as commonly specified in UK agreements satisfied the requirements of Regulation 1984/83 by referring to brands not types of beer.²⁸⁸ Secondly, extensive litigation was initiated in the UK due to the price differential between beer sold in free houses and tied houses as reflected in the

²⁸³ J Spicer et al, *Intervention in the Modern UK Brewing Industry* (Hampshire, Palgrave Macmillan, 2012) at p146 citing OFT Press release No. 4/95 'Enquiry into brewers' wholesale pricing policy', 7th February 1995

²⁸⁴ In December 1994, the Commission advised IEL that due to the complaints received it was reconsidering whether or not to grant exemption (above, n.283 at p146-147). The OFT believed brewers were charging their free trade customers a difference in wholesale prices of approximately £200 a barrel. P Rodgers, 'Beer Prices to fall as OFT opens inquiry' (*The Independent*, 8th February 1995)

<<http://www.independent.co.uk/news/business/beer-prices-to-fall-as-oft-opens-inquiry-as-oft-inquiry-start-1572064.html>> accessed 29th April 2015

²⁸⁵ Above, n.283 at p148

²⁸⁶ R Hotten, 'Brewers Cleared of Price Bias' (*The Independent*, 17th May 1995) quoting Bryan Carsberg, then OFT Director General <<http://www.independent.co.uk/news/business/brewers-cleared-of-price-bias-1619902.html>> accessed 5th July 2015

²⁸⁷ Commission Decision of 16 June 1999 in Case IV/36.081/F3 *Bass* ([1999] OJ L186/1); Commission Decision of 16 June 1999 in Case IV/35.992/F3 *Scottish and Newcastle* ([1999] OJ L186/28); and Commission Decision of 24 February 1999 in Case IV/35.079/F3 *Whitbread* ([1999] OJ L88/26)

²⁸⁸ N Von Hinten-Reed, 'UK Beer Cases' (1999) ECCPN (3) 38. 'Commission decision Whitbread pub leases – U.K. pub beer ties – not covered by block exemption – retroactive exemption granted' (1999) 20(5) E.C.L.Rev N75 at N75. This had been the source of confusion in the UK courts. The UK Court of Appeal considered whether the beer tie had to be by brand or by type in *Greenall Management Ltd v. Canavan (No.2)* ([1998] Eu LR 507) Millet L.J. was satisfied that Regulation 1984/83 was complied with where the drinks subject to the tie were specified by type, without a requirement for the brand or trademark to be specified. (*Greenall Management Ltd* [1998] Eu. LR 507 at p514). By contrast L.J. Staughton expressed some reservations over the ability of the brewer to unilaterally extend the list of drinks affected by the tie, contrary to the CJEU's ruling in *Delimitis*. (*Greenall Management Ltd* [1998] Eu LR 507 at p515) Clarification on this point was required.

Commission's foregoing request to the OFT to investigate the matter.²⁸⁹ Consequently, although the Commission considered that access to the relevant market for new and foreign brewers was considerably hindered and that the agreements of the brewers in question significantly contributed to that foreclosure, the notified leases were exempted under Article 101(3) TFEU. While tied lessees of all three paid more for beer than their free-of-tie competitors,²⁹⁰ the Commission concluded that the price differential is "*more than offset by quantifiable countervailing benefits*."²⁹¹ The 'average' tied lessees, on an overall assessment of their business relationship with the tying brewer was able to "*compete on a 'level playing field' with his free-trade counterpart*."²⁹² Amongst others, the Scottish & Newcastle tenants paid a lower rent which was considered to more than compensate for the price differential,²⁹³ the Bass tenants were similarly compensated by a rent subsidy and bulk buying and procurement services; and Whitbread's tenants were considered to be compensated by lower rent and apparently valuable business advice. In dealing with the UK practice of specifying beer by type rather than brand in the tying provision, contrary to Article 6(1) of Regulation 1984/83 noted above, the Commission stated its acceptance of this practice. As already noted in the CJEU's decision in *Delimitis* one of the purposes of limiting the purchasing obligation to beers specified within the tying agreement was to avoid brewers widening the tie, with implications for consumer choice and market foreclosure. By specifying beers by type, brewers are able to unilaterally extend, delete or substitute the brands of beer supplied by amending their price lists. Contrary to the terms of Article 6 of Regulation 1984/83 and the CJEU's judgment in *Delimitis*, the Commission, considered this to be a practical approach and made it easier for foreign beers to be introduced to national brewers' price lists.²⁹⁴ Tenants had long been opposed to tying by type as it distorted the commercial balance of the agreement, while brewers naturally preferred this.²⁹⁵ Further, the Commission considered that a relatively long-term exemption

²⁸⁹ N Von Hinten-Reed, 'UK Beer Cases' (1999) ECCPN (3) 38 at 38

²⁹⁰ For example, *Bass* [1999] OJ L186/1 at para 179, 24; *Scottish and Newcastle* [1999] OJ L186/28 at para 148, 49; *Whitbread* [1999] OJ L88/26 at para 161, 53

²⁹¹ *Bass* [1999] OJ L186/1 at para 186, 25; *Scottish and Newcastle* [1999] OJ L186/28 at para 155, 50; *Whitbread* [1999] OJ L88/26 at para 168, 54. Following its initial assessment of the price differential and countervailing benefits under the notified leases, the Commission published Notices in respect of each lease. See *Whitbread* [1997] OJ C294/2. This attracted 135 observations, 92 of which were to be treated as formal complaints. *Bass* [1998] OJ C36/5. This prompted 26 observations that were also to be treated as complaints. *Scottish and Newcastle* [1998] OJ C8/4 which received 16 observations that were also to be treated as complaints. Above, n.289 at p38.

²⁹² *Bass* [1999] OJ L186/1 at para 186, 25; *Scottish and Newcastle* [1999] OJ L186/28 at para 155, 50; *Whitbread* [1999] OJ L88/26 at para 168, 54

²⁹³ *Scottish and Newcastle* [1999] OJ L186/28 at para 155, 50

²⁹⁴ *Bass* [1999] OJ L186/1 at para 171, 23; *Scottish and Newcastle* [1999] OJ L186/28 at para 140, 48; *Whitbread* [1999] OJ L88/26 at para 153, 52

²⁹⁵ Above, n.62 at 290

period for the notified leases was justified in order to provide the brewers with legal certainty and to make commercial decisions.

Whilst aspects of the Commission's reasoning is difficult to reconcile with *Delimitis* and the terms of Regulation 1984/83, in 2001 in cases *Shaw*²⁹⁶ and *Joynson*,²⁹⁷ the General Court upheld the Commission's decisions to retroactively exempt the Whitbread and Bass leases. At the outset of its decisions, the Commission had started from the position that, in line with Regulation 1984/83, exclusive beer supply agreements generally resulted in improvements in distribution, but also acknowledged that such improvements would not materialise where the lessee was subject to unjustified price discrimination.²⁹⁸ On challenging the Commission's decision the applicants sought annulment of its decision to grant Whitbread and Bass individual exception under Article 101(3) TFEU. In *Shaw* the applicants opposed the Commission's finding that whilst Whitbread's tenants suffered price discrimination, this was compensated by countervailing benefits enjoyed by tied tenants.²⁹⁹ They contested that the price differential was greater than that established by the Commission and the countervailing benefits enjoyed by tenants were less extensive than the Commission had found in its judgment.³⁰⁰ It was also asserted that from 1990-1994, the Whitbread lease failed to provide sufficient countervailing benefits to fully compensate tenants for the price differential.³⁰¹ Nevertheless, the General Court upheld the Commission's decision and so approved of the Commission's assessment of the countervailing benefits enjoyed by Whitbread's tenants, noting the Commission's "*painstaking investigation*" into the issue of the price differential.³⁰² Whilst tenants had not

²⁹⁶ (T-131/99) *Shaw v Commission* [2002] ECR II-2023, [2002] 5 CMLR 81. Concerned the Whitbread lease.

²⁹⁷ (T-231/99) *Joynson v Commission* [2002] ECR II 2085, [2002] 5 CMLR 123. Concerned the Bass lease.

²⁹⁸ (T-231/99) *Joynson v Commission* [2002] 5 CMLR 124 at para 39-42, p135. The Court highlighted that the Commission had noted that price discrimination played an important role in the economic justification for exemption of exclusive purchasing obligations. This was due to the fact that purchasers are unable to resort to alternative sources of supply for the duration of the agreement, unlike other customers of the producer. (*Joynson* [2002] 5 CMLR 123 at para 40, p135)

²⁹⁹ (T-131/99) *Shaw v Commission* [2002] 5 CMLR 81 at para 56-57, p97. The Commission also found that tied lessees faced with unjustified price differentials may be unable to compete on equal terms, however, as in *Joynson* such price differentials only has a negative effect on the competitiveness of the tied lessee where it was significant and long lasting (*Joynson* [2002] 5 C.M.L.R. 123 at para 43-44, p135-136).

³⁰⁰ (T-131/99) *Shaw v Commission* [2002] 5 CMLR 81 at para 57, p97. In *Shaw* it was claimed that the price differential relied on by the Commission "*bears no relation to the realities of the market*" which is only made up of a small number of independent wholesalers and that breweries, such as Whitbread, act as wholesalers to free houses and allowed them large discounts which were not accounted for. (*Shaw* [2002] 5 CMLR. 81 at para 62, p98) The Commission's reference group was also considered to be too restricted a sample. It only included individual free houses and excluded pubcos despite their significant share of the retail market. It also failed to include managed public houses and clubs which all competed with Whitbread's tied houses. (*Shaw* [2002] 5 CMLR 81 at para 63, p97) The Court however found that individual free house operators were the only operators at the same level of distribution as Whitbread's tied houses and so a reliable comparison could be made with those lessees. (*Shaw* [2002] 5 CMLR 81 at para 69, p97)

³⁰¹ *Ibid* at para 84, p101

³⁰² *Ibid* at para 76, p100. P Bridgeland, 'New case law on market foreclosure. Court of First Instance upholds three Commission decisions relating to beer ties' (2002) (2) ECCPN 45 at p46

been fully compensated for the price differential in the first three years of the majority of the leases entered into, the Court upheld the Commission's exemption of Whitbread's leases for their entire duration.³⁰³ In doing so, it approved of the Commission's conclusion that a brewer's price discrimination would only have a significant negative impact on competitiveness of a tied lessee if it was both significant and long-lasting.³⁰⁴ This was not deemed to be so under the Whitbread lease, with the Court highlighting the Commission's finding that in the first three years of the lease the price differential was only £3-£6 per barrel of the beer price and tied lessees also shared in 'unquantifiable' countervailing benefits resulting from being tied to Whitbread as opposed to being a free house.³⁰⁵ Similarly in *Joynson*, on challenging the Commission's decision regarding the Bass lease, the applicants asserted that the Commission in excepting the lease under Article 101(3) TFEU made "*manifest errors*" in its assessment by failing to take sufficient account of the profitability of Bass's tied houses and in its assessment of the price differential, rent subsidy and the countervailing benefits for tied lessees.³⁰⁶ However, as in *Shaw*, the Court again rejected all of these arguments. It approved of the Commission's assessment of all of the points highlighted by the applicants, finding that it had correctly focused not on the issue of the profitability of Bass's tied pubs by comparison to its competitors, but on the issue of whether tied lessees faced significant and long-term price discrimination.³⁰⁷ Consequently, the Commission's handling of beer tie agreements whilst producing reasonably controversial results for the reasons discussed above, was met with the approval of the General Court.

3. Reform – the need for a more economic approach to the treatment of vertical agreements

While the Commission and the Courts proceeded with their decisional practices discussed above, on-going discontent over Regulation 1984/83 prompted calls for a more economic approach to the treatment of all categories of vertical agreements. As noted above Korah and Rothnie were critical of Regulation 1984/83's sector-specific rules from the outset as they were ignorant of economic considerations and too interventionist.³⁰⁸ The Commission had also received numerous complaints regarding the interpretation and application of the

³⁰³ Above, n.300 at para 204-205, p119

³⁰⁴ Ibid at para 211, p120. P Bridgeland, (2002) (2) ECCPN 45 at p47

³⁰⁵ Above, n.300 at para 191, p117. P Bridgeland, (2002) (2) ECCPN 45 at 74

³⁰⁶ Above, n.298 at para 38, p135

³⁰⁷ Ibid at para 51, p137-138. P Bridgeland, (2002) (2) ECCPN 45 at 74

³⁰⁸ Above, n.16 at para 8.1, p201

sector specific rules of Regulation 1984/83.³⁰⁹ Maitland-Walker states that issues regarding the interpretation of the provisions were to be expected given the reliance placed on subjective terms such as ‘more favourable conditions’.³¹⁰ Such subjectivity causes legal uncertainty which in turn undermines the usefulness of the Regulation. It prompted complaints to the Commission and subsequently defeated one of the primary reasons for the adoption of the Regulation, namely to reduce the Commission’s individual examination of agreements.³¹¹

In addition to these specific problems with Regulation 1984/83, EU law on vertical agreements generally had been subject to significantly more criticism than any other aspect of EU competition law.³¹² The list of widely held complaints included that the law was not only too formalistic, but was overly ‘clause-based’ and lacked a suitably economic approach in determining whether or not competition is restricted.³¹³ Hawk, in his scathing attack on the EU’s approach towards vertical agreements and its over-broad application of Article 101(1) TFEU to them, highlighted the inadequate economic analysis under Article 101(1) TFEU; an unconvincing rationale for the overbroad application of Article 101(1) TFEU, noting in particular the notion of economic freedom; and the Commission’s ongoing resistance of Court judgments adopting a more economics-based approach.³¹⁴

Given the mounting pressure of such criticism on the Commission and the looming expiry of the BERs³¹⁵ in December 1997, it eventually acknowledged the failings of the system and undertook its reform.³¹⁶ Early in 1997 the Commission published its Green Paper on vertical restraints.³¹⁷ Many shortcomings of EU competition policy concerning vertical restraints were acknowledged, with a Communication being published by the Commission

³⁰⁹ Commission of the European Communities, *Seventeenth Report on Competition Policy* (1988, Brussels), para 29, p35

³¹⁰ J Maitland-Walker, ‘Editorial, The Seventeenth Report on Competition Policy’ (1988) 9(3) E.C.L.Rev 253 at 253

³¹¹ Ibid at p253-254

³¹² R.P. Whish, ‘Recent Developments in Community Competition Law 1998/1999’ (2000) 25(3) E.L. Rev 219 at 227

³¹³ Ibid at 227

³¹⁴ B Hawk, ‘System Failure: Vertical Restraints and EC Competition Law’ (1995) 32(4) C.M.L.Rev 973 at 975. Hawk is also very critical of the notification system under Regulation 17/62. He highlights the overbroad application of Article 101(1) TFEU; resulting legal uncertainty; the proliferation of Block Exemption Regulations; legal formalism and analysis by categories; and a lack of economic analysis. (Ibid at 974)

³¹⁵ Regulations 1984/83 and 1983/83

³¹⁶ Above, n.9 at 283

³¹⁷ European Commission, Green Paper, *Vertical Restraints in EC Competition Policy*, COM(96) 721 Final, published 22 January 1997, Hereinafter referred to as the ‘Green Paper’.

in 1998 summarising the responses to the Green Paper.³¹⁸ This created a framework for policy reform, and formed the basis for Regulation 2790/99.³¹⁹ The Commission intended its new policy on vertical agreements to create a more efficient system for the protection of competition, to remove the ‘strait-jacket’ effect of the current system and to reduce the enforcement costs on industry.³²⁰ In order to achieve this, the Commission identified four pillars on which its new policy was to be based. These included one broad umbrella BER applicable to both goods and services including a market share cap and a ‘black’ list approach; Guidelines on the Commission’s policy where the BER thresholds are exceeded and withdrawal of the exemption; reduced notification requirements through the amendment of Regulation 17 removing the Commission’s monopoly in applying Article 101(3) TFEU; and an increased role for National Competition Authorities (NCAs) and courts.³²¹ Whilst these proposals outlined an encouraging move towards an improved system for the handling of vertical agreements in the EU, there were concerns amongst industry that the proposals were too complex and that the use of market share thresholds would reduce the legal certainty of the proposed regime.³²²

3.1 Regulation 2790/99

On 1 June 2000, Regulation 2790/99 on vertical agreements and concerted practices³²³ came into force thereby replacing Regulation 1984/83 and Regulation 1983/83 BERs with a single umbrella Regulation. This brought about three principal changes this brought about. These were a broader scope of application of the BER; a more economics-based approach, considering the market power of the undertakings concerned; and the *per se* prohibition of certain restrictions, through the maintenance of the black list approach.³²⁴ In its Communication, discussed above, the Commission had made clear its intention to move from its ‘form-based requirements’ with ‘sector-specific rules’ towards a system based on economic effects, focusing on almost all sectors of distribution, through the adoption of a

³¹⁸ European Commission, *Communication from the Commission on the application of the Community competition rules to vertical restraints (Follow-up to the green paper on vertical restraints)* (1998) OJ C365/3. 227 written submissions were received in response to the green paper. The majority of these highlighted that the current system was too legalistic and favoured a more economics-based approach. Amongst others, the current approach was deemed to inhibit new and innovative distribution formats that could result in efficiency gains. (Ibid at para 1, p5)

³¹⁹ Above, n.11 at p60

³²⁰ Above, n.318 at para 4, p23

³²¹ Ibid at para 4, p23

³²² D Cowan and J Nazerali, ‘The Commission’s draft Communication on distribution agreements – market shares are predictably back on the table!’ (1998) 19(7) E.C.L.Rev 409 at 412-413

³²³ Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices (1999) OJ L336/21

³²⁴ Above, n.17 at p639

single Regulation.³²⁵ This also signalled the end of the sector specific rules of Regulation 1984/83. The Commission noted that in order to ensure ‘coherence and unity of policy’, those rules dealing specifically with beer supply agreements under Title II of Regulation 1984/83 had to be withdrawn.³²⁶ There was no longer a legal or economic justification for their continuation and to the extent that sector-specific treatment was justified, the Guidelines would cover this.³²⁷ Regulation 2790/99 was applicable to all vertical restraints concerned with intermediate and final goods, as well as services, with the exception of only a few hardcore restraints. Shortly after its implementation, in October 2000, the Commission published Guidelines on the application of the new BER.

3.1.1 The extended exemption

In light of the aforementioned considerations, Regulation 2790/99 consolidated the provisions dealing with all vertical agreements and so was a significant development for EU competition law. Through the definition of vertical agreements and vertical restraints in Article 2(1) of Regulation 2790/99 its scope was extended beyond that of its predecessors. It stated that:

“Article [101](1) TFEU] shall not apply to agreements or concerted practices entered into between two or more undertakings each of which operates for the purposes of the agreement, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services (‘vertical agreements’).

This exemption shall apply to the extent that such agreements contain restrictions of competition falling within the scope of Article [101](1) TFEU] (‘vertical restraints’).”

This definition consisted of three main elements. Firstly, the agreement or concerted practice could be between two or more undertakings, in comparison to previous Regulations, which restricted exemption to bilateral agreements between undertakings.³²⁸ Secondly, the undertakings have to be operating, for the purpose of the agreement, at

³²⁵ The only exception to this was the distribution of cars, which was dealt with under a BER that was not due to expire until 2002. Above, n.318. Also European Commission, XXVIIIth Report on Competition Policy 1998, SEC(99) 743 FINAL at para 36, p29.

³²⁶ European Commission, XXVIIIth Report on Competition Policy 1998, SEC(99) 743 FINAL at para 47, p31. As will be discussed in Chapter 6, those of Title II were also withdrawn.

³²⁷ European Commission, XXVIIIth Report on Competition Policy 1998, SEC(99) 743 FINAL at para 47, p31

³²⁸ European Commission Notice, *Commission Guidelines on Vertical Restraints* (2000) OJ C291/1 at para 24, p7

different levels of the production or distribution chain.³²⁹ Thirdly, the agreement has to concern the conditions under which the parties ‘may purchase, sell or resell certain goods or services’, thereby reflecting the Regulation’s purpose, namely to include both purchasing and distribution agreements.³³⁰ Exemption was no longer limited to the supply of goods for resale. All final and intermediate goods and services were covered. Consequently, subject to the other provisions of the Regulation, it was capable of application to all types of vertical agreements, including those in the beer and petrol industries. However, Article 2(4) clarified that as before the exemption provided for in Article 2(1) was not applicable to ‘vertical agreements entered into between competing undertakings’ thereby limiting restrictions of inter-brand competition. Article 2(5) also provided that the exemption did not apply where the vertical agreement fell within the scope of another BER.

3.1.2 Economics-based approach

In keeping with the Commission’s intention to adopt a more economics-based approach, the preamble to Regulation 2790/99 stated that the likelihood of the efficiency enhancing effects of vertical restraints outweighing any anticompetitive effects, depends on the degree of market power of the undertakings and so the level of competition they face from competing suppliers.³³¹ Recital 8 stated that, where the market share of the supplier does not exceed 30%, it can be presumed that vertical agreements which do not contain any of the ‘black’ listed provisions, generally lead to an improvement in production or distribution and allow consumers a fair share of the resulting benefit. Article 3 of Regulation 2790/99 therefore introduced a market share cap for the first time. This provided that the Article 2 exemption would only apply where the market share held by the supplier did not exceed 30% of the relevant market on which it sells the contract goods or services. The intention was that this would prevent other suppliers being foreclosed from accessing customers.³³² However, Article 2(3) provides that where a vertical agreement contains an exclusive supply obligation,³³³ the buyer, not the supplier’s, market share must not exceed 30% of the relevant market on which it purchases the contract goods or services. This was intended to prevent competing buyers being foreclosed from suppliers. However, Article 3 also marked an attempt to address criticisms regarding the over-

³²⁹ Ibid at para 24, p7

³³⁰ Ibid at para 24, p7

³³¹ Recital 7 of Regulation No 2790/1999

³³² Recital 12, Regulation 2790/99. Article 9 dealt with the market share calculation.

³³³ Article 1(c), Regulation 2790/99 defines exclusive supply obligation as “*any direct or indirect obligation causing the supplier to sell the goods or services specified in the agreement only to one buyer inside the Community for the purposes of a specific use or for resale*”.

application of Article 101(1) TFEU and so responded to the argument that vertical agreements are only harmful where the parties possess market power.³³⁴ It also dispensed with the sector-specific rules of Regulation 1984/83 which had been criticised for their formalism and lack of economic considerations.³³⁵ The new market share cap would therefore impact on those large breweries and pubcos which had previously complied with, and so enjoyed exemption under Regulation 1984/83 despite their significant market shares.

Despite its more economic focused approach, the market share test of Regulation 2790/99 was contrary to the prevailing wishes of industry.³³⁶ Nevertheless, the Commission considered it was the only reliable gauge of market power, noting that “[n]obody has been able to suggest a better single indicator than market share for use in a block exemption regulation.”³³⁷ The implementation of the market share approach prompted concerns to be raised. There were concerns over adequacy of the 30% threshold. Whish and Bailey remark on it being generous and providing a safe harbour for hundreds if not thousands of agreements.³³⁸ Industry however was in favour of a 40% threshold.³³⁹ Many concerns also focused on the reliability of calculating market shares due to the difficulty in defining the relevant market for the products in question, an analysis which Bortolotti rightly highlights is largely subjective and so can cause uncertainty.³⁴⁰ However, Whish notes that the uncertainty generated by the market share threshold would not cause the Commission to be inundated with notified agreements due to procedural changes removing notification as a requirement for individual exemption.³⁴¹ Bishop and Ridyard also support its introduction stating that the rationale behind it is “*sound and is intended to eliminate the regulatory burden on firms that, to put it starkly, could not behave in anti-competitively even if they tried.*”³⁴² However, they acknowledge the use of the market share cap in the BER imposes an “*undue weight*” on the definition of the relevant market.³⁴³ This position is supported by

³³⁴ Above, n.17 at p650

³³⁵ Above, n.16 at para 8.1, p201. D Cowan and J.S. Nazerali, ‘Reforming EU distribution rules- has the Commission found vertical reality?’ (1999) 20(3) E.C.L.Rev 159 at 262

³³⁶ The Commission was aware of this prior to its implementation of regulation 2790/99. Above, n.318 at para 1, p5

³³⁷ Ibid at para 2, 15

³³⁸ R Whish and D Bailey, *Competition Law* 7th Edition (Oxford, Oxford University Press, 2012) at p660

³³⁹ Above, n.322 at 411

³⁴⁰ F Bortolotti, ‘The revision of the block exemptions on vertical restraints: a critique of the Commission’s market share approach’ (1999) 2 I.B.L.J. 207 at 216-217

³⁴¹ This was by virtue of Council Regulation (EC) No 1216/1999 of 10 June 1999 amending Regulation No 17: first Regulation implementing Articles 81 and 82 of the Treaty (1999) OJ L148/5. R Whish, ‘Recent developments in Community Competition law 1998/1999’ (2000) 25(3) E.L. Rev 219 at 229

³⁴² S Bishop and D Ridyard, ‘E.C. Vertical restraints guidelines: effects based or per se policy?’ (2002) 23(1) E.C.L.Rev 35 at 35

³⁴³ Ibid at 37

Waelbroeck who highlights that although the market share criterion was a significant improvement on the formalistic approach of the past, such criterion are necessarily arbitrary and provide only ‘imperfect guidance’ regarding the actual problems that agreements cause in reality.³⁴⁴ He correctly highlights the problem that some agreements may require to be scrutinised even below the 30% threshold, however, benefit from exemption.³⁴⁵ Likewise, agreements above the threshold may be deprived the certainty of exemption, despite being inoffensive.³⁴⁶ Consequently, Waelbroeck questions the need for market share thresholds at all, stating that as long as there was sufficient inter-brand competition in the relevant market, it was unlikely that the restraint would have a significant impact on competition.³⁴⁷ However, Bishop and Ridyard arguably propose a better solution to the problem of such flawed decisions. They highlight that these could be limited by placing reduced emphasis on market definition and market share calculations by performing a more detailed assessment of the actual competitive effects of the vertical restraint in its particular context.³⁴⁸ Nevertheless, it is submitted that whilst excessive reliance may be placed on market share thresholds in Regulation 2790/99, their introduction marked a significant progression in the EU’s move towards an effects-based approach to competition law with Bishop and Ridyard supporting this position.³⁴⁹

The Commission’s Guidelines on vertical restraints, published shortly after Regulation 2790/99, also clarified the Commission’s approach where the 30% market share threshold was exceeded. Under those circumstances there was no presumption of illegality but individual exception may be necessary.³⁵⁰ The Guidelines were intended to assist companies in determining whether their agreements benefitted from exemption under Regulation 2790/99 or whether their agreement satisfied the requirements of Article 101(3) TFEU without notifying the Commission. In determining the latter, they provided a framework of analysis and divided vertical agreements into four categories in order to analyse their possible negative effects.³⁵¹ Beer supply agreements, like and service station agreements, were classified as single branding agreements as their main element was the buyer being required to concentrate his orders for a certain type of product with the one

³⁴⁴ D Waelbroeck, ‘Vertical agreements: 4 years of liberalization by regulation n.2790/99 after 40 years of legal (block) regulation’ in H Ullrich, ed, *The Evolution of European competition Law Whose Regulation, Which Competition?* (Cheltenham, Edward Elgar Publishing, 2006) at p87

³⁴⁵ Ibid at p87

³⁴⁶ Ibid at p87

³⁴⁷ Ibid at p90

³⁴⁸ S Bishop and D Ridyard, ‘E.C. Vertical restraints guidelines: effects based or per se policy?’ (2002) 23(1) *E.C.L.Rev* 35 at 37

³⁴⁹ Ibid at 35

³⁵⁰ Above, n.328 at para 62, 14

³⁵¹ These were: a single branding group; a limited distribution group; a resale price maintenance group; and a market partitioning group. (Ibid at para 104, p21)

supplier.³⁵² The Guidelines noted four principle negative effects on competition resulting from such agreements. These included the risk of foreclosure of the market to other suppliers; increased rigidity in market shares thereby aiding collusion when applied by several suppliers; lack of in-store inter-brand competition; and the buyer having to pay a higher price for tied products.³⁵³ The Guidelines also highlighted the reduction in inter-brand competition due to such agreements may be alleviated by the initially strong competition between suppliers to obtain the contract, however, the longer the duration of such agreements, the less it is likely that this initially strong competition will be enough to compensate for the reduction in inter-brand competition.³⁵⁴ The Guidelines also acknowledged the many positive effects of vertical restraints generally.³⁵⁵ These factors to be considered in determining whether the agreement in question infringed Article 101(1) TFEU are noted to include amongst others the market position of the supplier and their competitors; entry barriers; maturity of the market; and the level of trade.³⁵⁶ Subsequently the Guidelines appeared to represent a more economic approach to the assessment of vertical agreements by the Commission.

In light of the foregoing, the notification requirements were greatly reduced under the new regime. However inevitably there were still occasions where the market share cap was breached and individual exception sought. This was exemplified by Interbrew, Belgium's largest brewer, notifying its supply agreement with on-trade establishments in Belgium to the Commission.³⁵⁷ Their agreement had to be amended before being approved by the Commission. This would not have been necessary under Regulation 1984/83 due to the safe harbour it provided for brewers' agreements irrespective of their market share.³⁵⁸ Nevertheless in doing so, the Commission still ultimately accepted significant non-compete obligations despite Anheuser Busch InBev's market share of 53%.

Under the new regime, the Commission's decisional practice therefore appeared to continue largely as before through the continued approval of beer supply agreements. This is not to say that the outcome is wrong, it simply serves to highlight the Commission's perseverance in ensuring the approval of agreements within this sector. However, given the significant market position of Interbrew and the concerns expressed over their non-

³⁵² Ibid at para 106, p21

³⁵³ Ibid at para 107, p21

³⁵⁴ Ibid at para 108, p21

³⁵⁵ Ibid at p22-24

³⁵⁶ Ibid at para 121, p26

³⁵⁷ European Commission, *Notice published pursuant to Article 19(3) of Regulation 17 concerning notification COMP/A37.904/F3 – Interbrew* (2002) OJ C283/14. This is discussed further in Chapter 5.

³⁵⁸ Press Release, 'European Commission opens up Interbrew's horeca outlets to competing beer brand' (15th April 2003) Brussels IP/03/545

compete obligations, it may have been prudent for the Commission to undertake to review the operation of its revised agreements after a period of years. This would have enabled it to assess whether or not the commitments offered were having the desired effect in opening up the relevant markets to increased competition. Nevertheless, it is accepted that Article 3 of Regulation 2790/99 marked a significant step towards a more economic-based approach by recognising the link between market power and the effect of restraints, thereby requiring amendments to agreements that would not have been necessary under Regulation 1984/83.

3.1.3 De-minimis

While as noted above the industry expressed concerns over the introduction of the market share cap in Regulation 2790/99, this was not the only market share threshold to be taken into consideration when assessing vertical agreements, including those in the brewing industry. Shortly after the adoption of Regulation 2790/99, the Commission published a new *de minimis* Notice.³⁵⁹ This was considered necessary to ensure ‘coherence’ between the new Regulation 2790/99 and the *de minimis* notice.³⁶⁰ Through this the Commission used market share thresholds as a means to quantify what is not an appreciable restriction on competition for the purposes of Article 101(1) TFEU. The *de minimis* Notice showed a slight relaxation towards vertical agreements. Part II of the Notice stated that they did not appreciably restrict competition for the purpose of Article 101(1) TFEU where the agreement was between undertakings which are not actual or potential competitors on the markets affected and the market share held by each party to the agreement did not exceed 15% of any of the relevant markets affected by the agreement.³⁶¹ This was an increase on the 5% threshold under the Commission’s 1986 *de minimis* Notice.³⁶² It also dispensed with the turnover test. Under the 1986 Notice the Commission had established an ECU 300 million turnover threshold below which undertakings were able to benefit from the

³⁵⁹ European Commission, *Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty Establishing the European Community (de minimis)* (2001) OJ C368/13

³⁶⁰ L Peeperkorn, ‘New Notice on agreements of minor importance (de minimis notice)’ (2002) (1) ECCPN 45 at 45

³⁶¹ Above, n.359 at para 7(b), p13. The market share threshold for parties to a horizontal agreement were set at 10% as these were considered to have a greater restrictive effect on competition (ibid at para 7(b), 13).

Also S Rating, ‘Commission proposes new *de minimis* notice’ (*Europa*, 1st April 1997) <http://ec.europa.eu/competition/speeches/text/sp1997_017_en.html> accessed 18th February 2015

³⁶² European Commission, *Notice of 3 September 1986 on agreements of minor importance which do not fall under Article 85(1) of the Treaty establishing the European Economic Community* (1986) OJ C231/2 as later amended by European Commission, *Notice concerning the updating of the 1986 communication on agreements of minor importance* (1994) OJ C368/20 (hereinafter referred to as the 1986 Notice). This superseded the Commission’s 1977 *de minimis* Notice

Notice.³⁶³ By dispensing with this threshold, the Commission denied SMEs preferential treatment over larger undertakings as it was no longer turnover but the market position of the contracting parties that governed whether there was an appreciable restriction on competition.³⁶⁴ The new 15% threshold therefore opened up the *de minimis* safe harbour to more beer supply agreements. However, in line with CJEU's judgment in *Delimitis*, discussed above, the Notice made provision for the 'cumulative foreclosure effect of parallel networks of agreements having a similar effect on the market'. This was a heightened risk in the beer, as well as the petroleum, market due to the widespread reliance on exclusive purchasing agreements within these discussed above. Such a cumulative foreclosure effect was considered unlikely where less than 30% of the relevant market was covered by parallel agreements having similar effects; and individual suppliers or distributors were not considered to contribute significantly to the foreclosure effect where their market share did not exceed 5%.³⁶⁵ Therefore where competition in the relevant market was restricted due to the cumulative effect of such agreements, the market share thresholds under paragraph 7 of the Notice were reduced to 5% for both horizontal and vertical agreements.³⁶⁶ Consequently, despite the difficulties in calculating market shares, discussed above, they were central to the regime applicable to vertical agreements. However, the Notice also clearly listed the hardcore restrictions the inclusion of which deny vertical agreements exemption even where the market share thresholds are met.³⁶⁷ These reflected those contained in Regulation 2790/99.

3.1.4 The 'black' list

In keeping with the regime under Regulation 1984/83, Article 4 of Regulation 2790/99 detailed the 'black' list of restrictions. However, these were referred to as 'hardcore' restrictions, the inclusion of which denied the agreement exemption.³⁶⁸ These were illegal, regardless of the market shares of the parties, and due to their *per se* illegality, no economic analysis was required to determine their validity.³⁶⁹ They differed from the five 'black' clauses listed in Regulation 1984/83 discussed above. Firstly, Article 4(a) was

³⁶³ European Commission, *Notice of 3 September 1986 on agreements of minor importance which do not fall under Article 85(1) of the Treaty establishing the European Economic Community* OJ (1986) C231/2 as amended at para 7, p2-3

³⁶⁴ S Rating, 'Commission proposes new *de minimis* notice' (*Europa*, 1st April 1997) <http://ec.europa.eu/competition/speeches/text/sp1997_017_en.html> accessed 18th February 2015

³⁶⁵ Above, n.359 at para 8, p14

³⁶⁶ Ibid at para 8, p14

³⁶⁷ Ibid at para 11, p14

³⁶⁸ The Commission's Guidelines on Vertical Restraints made it clear that there was no option of severability for the prohibited clauses. The whole of the vertical agreement would be outwith the BER. It also stated that individual exception of agreements containing such hardcore restrictions was unlikely. Above, n.328 at para 46, p11

³⁶⁹ Above, n.11 at p104

concerned with resale price maintenance,³⁷⁰ due to its market partitioning potential through the division of national markets, and prohibited the seller from determining the minimum sales price.³⁷¹ Article 4(b), similarly to Article 2(c) of Regulation 1984/83, focused on restrictions on territory and customers and prohibited absolute territorial protection, with some exceptions.³⁷² This prohibition related back to the Commission's long held integration objectives.³⁷³ Thirdly, Article 4(c) sought to ensure parallel trade, where selective distribution systems were utilised;³⁷⁴ with the fourth and fifth restrictions also focused on these.³⁷⁵

However, Article 5 of Regulation 2790/99 introduced a new 'grey' list, namely clauses which were denied coverage by the BER but were severable from the remainder of the agreement.³⁷⁶ The first such 'grey' clause was detailed in Article 5(a) and addressed non-compete obligations as are common in beer supply agreements.³⁷⁷ Exemption was denied to such obligations of indefinite duration or in excess of 5 years. Where the obligation was tacitly renewable beyond the initial five-year period it was deemed to have been concluded for an indefinite duration. This reflected the Commission's long held concern over the duration of such obligations and their foreclosure effects. However, in keeping with the deference of the past, the Commission was careful to ensure that the beer supply agreements under which the goods were sold from premises and land owned or leased by the supplier continued to benefit from exemption. This potentially avoided the wrath of the powerful lobbyists who had largely influenced past policy. All that was prohibited was for the non-compete obligation to exceed the period of occupancy of the premises and land by the buyer.³⁷⁸ The CJEU however clarified that Regulation 2790/99 clearly required that the supplier owned both the land and the premises from which the contractual goods were sold by the reseller before exemption could be granted, thereby tightening up on the provisions under Regulation 1984/83.³⁷⁹

³⁷⁰ The Guidelines define this as 'agreements or concerted practices which have as their direct or indirect object the establishment of a fixed minimum price level to be observed by the buyer'. Above, n.328 at para 47, p11

³⁷¹ Ibid at para 47, p11

³⁷² Above, n.328 at para 49, p11

³⁷³ Above, n.11 at p105

³⁷⁴ Article 4(c)

³⁷⁵ These are not considered here as they are not of relevance to beer supply agreements

³⁷⁶ Above, n.328 at para 57, p13

³⁷⁷ The Guidelines define these as 'obligations requiring the buyer to purchase from the supplier or an undertaking designated by it, more than 80% of the buyer's total purchases during the previous year of the contract goods or services and their substitutes thereby denying the purchaser the ability to purchase competing goods or services.' Above, n.328 at para 58, p13

³⁷⁸ Article 5 Regulation 2790/99

³⁷⁹ (C-260/07) *Pedro IV Servicios SL v. Total España SA* [2009] ECR I-2437; [2009] 5 CMLR 1291 at para 44, p1331. See Chapter 6.

The CJEU noted that the Commission had changed the condition for exemption in order to prevent the maximum duration for exclusivity clauses fixed by the Regulation being circumvented.³⁸⁰ However, in its Guidelines, the Commission sought to justify the continuation of the exemption of such arrangements simply on the basis that it would be unreasonable to expect a supplier to allow competing products to be sold from the premises owned or let by him, without his permission.³⁸¹ Consequently, even in the absence of the sector-specific rules of Regulation 1984/83 the beer supply and ultimately service station agreements continued to benefit from exemption, albeit as more narrowly construed by the CJEU. This was notwithstanding the concerns surrounding exclusive purchasing obligations of long duration which prompted the Commission to limit the duration of such obligation to five-years in most other sectors of the economy where the special conditions of Article 5(a) regarding supplier owned or let premises and land were unlikely to be met.³⁸²

3.1.5 Withdrawal of the Regulation

Article 6 of Regulation 2790/99 also made provision to address the situation where inter-brand competition on a relevant market was weak or restricted by allowing the Commission, in certain circumstances, to withdraw the benefits of the BER. This presented potential implications for the beer industry which is prone to parallel networks of agreements and their cumulative effects, as this was a ground for such withdrawal.³⁸³ Recital 13 made clear that withdrawal could occur ‘where parallel networks of vertical agreements have similar effects which significantly restricted access to a relevant market or competition therein’.³⁸⁴ It noted that this was likely to occur in the case of non-compete obligations, as in *Langnese*,³⁸⁵ the only case to date where the benefit of the BER has been withdrawn. Further, Article 6 stated that the Commission could withdraw the Regulation where it found ‘in any particular case’, rather than a ‘particular market’, that an agreement has effects that are incompatible with Article 101(3) TFEU. Article 7, which was unparalleled in Regulation 1984/83 also enabled NCAs to withdraw the benefit of the exemption where in any particular case, vertical agreements to which the Regulation

³⁸⁰ *Pedro IV Servicios SL* [2009] 5 CMLR 1291 at para 65, p1332-1333

³⁸¹ Above, n.328 at para 59, p14

³⁸² Article 5 made provision for other ‘grey’ restrictions. They are not considered here as unlike Article 5(a) they are not of the same relevance to beer supply agreements. The Second grey restriction concerned post-term non-compete obligations (Article 5(b)). The third concerned competing products in selective distribution systems (Article 5(c))

³⁸³ Article 6 of Regulation 2790/99

³⁸⁴ It also stated that this could occur where the buyer has significant market power in the relevant market in which it resells the goods or provides the services. See Recital 13 of Regulation 2790/99

³⁸⁵ Above, n.239

applied, had effects incompatible with Article 101(3) TFEU, ‘in a Member State, or in part thereof, which has all of the characteristics of a distinct geographical market’. However, Article 8 was similarly novel and provided for the disapplication of the BER by Commission Regulation where parallel networks of similar vertical restraints covered more than 50% of the relevant market, thereby restoring the full application of Articles 101(1) TFEU and 101(3) TFEU.³⁸⁶ Consequently, Regulation 2790/99 widened the scope for the possible withdrawal of the benefits of the BER, however, as noted above, this has only been successful in *Langnese*.

3.1.6 Reaction to the new rules

Regulation 2790/99 marked a significant progression in the Commission’s treatment of vertical agreements and so was generally welcomed. By moving away from the ‘white’ list approach, which was originally driven by the desire for legal certainty, it appeared to introduce some much need flexibility, leaving behind the ‘strait-jacket’ effect of Regulation 1984/83. Further, the adoption of the market share criterion was a move away from the formalistic approach of the previous regime, although as discussed above its implementation and 30% threshold were greatly criticised. Nevertheless, the introduction of market share thresholds was recognition of the link between the effects of the restraint in question and the market power of the undertakings concerned, and so agreements of major brewers, pubcos and oil companies no longer benefitted from block-exemption where the market share cap was exceeded. Whilst this represented a significant advancement in the treatment of vertical agreements, as discussed above, by virtue of Article 5(a), the time-limits imposed on non-compete obligations did not apply where the contract goods or services were sold by the buyer from premises and land owned or leased by the supplier. Therefore the new regime maintained the Commission’s deference towards beer supply agreements, despite the continued concerns over these in member states, such as the UK.

3.2 Regulation 330/2010

Notwithstanding the concerns discussed above, Regulation 2790/99 was still regarded as a ‘revolution’ in the treatment of vertical restraints.³⁸⁷ It was however set to expire on 31 May 2010. This prompted the Commission in July 2009 to issue a new draft Regulation

³⁸⁶ Above, n.328 at para 80-81, p17

³⁸⁷ Above, n.338 at p650

and Guidelines on supply and distribution agreements for public consultation.³⁸⁸ This acted as a review of the current system. The Commission noted that it considered the current regime to have worked well overall and did not propose to fundamentally alter it. It did however propose amendments to take into account recent market developments, especially the increased buyer power of big retailers and the growth of on-line sales.³⁸⁹ The Commission adopted Regulation 330/2010 on Vertical Agreements and Concerted Practices on 20th April 2010³⁹⁰ with this entering into force on 1 June 2010.³⁹¹ Accompanying Guidelines were published by the Commission in May 2010.³⁹² Whish and Bailey correctly note that the BER and Guidelines adopted by the Commission only represented a ‘mild evolution’ of the law, largely following the provisions of Regulation 2790/99, and accompanying Guidelines.³⁹³ Consequently, only the new provisions in Regulation 330/2010 regarding market share shall be considered here.³⁹⁴

3.2.1 New market share criterion

In light of the Commission’s perception that the regime under Regulation 2790/99 had worked well with it only being necessary to address the issue of progressively powerful retailers, Regulation 330/2010 extends the market share criterion first introduced by Regulation 2790/99 for determining whether or not an agreement should benefit from exemption. Whilst the inclusion of market share thresholds is now largely accepted, there was significant debate over the Commission’s decision to include such thresholds for both the buyer and the supplier.³⁹⁵ Article 3 states that for exemption to be granted, the market share held by the supplier does not exceed 30% of the relevant market on which it sells the contract goods or services and the market share of the buyer does not exceed 30% of the relevant market on which it purchases the contract goods or services. As discussed above, under Article 3 of Regulation 2790/99 the buyer’s market share was irrelevant except in the case of exclusive supply obligations. Recital 8 of Regulation 330/2010 states that where the market share thresholds are complied with by both undertakings, and the agreement does not include any hardcore restrictions detailed in Article 4 of the BER, it will usually lead to an improvement in production and distribution and allow consumers a

³⁸⁸ Press Release, ‘Antitrust: Commission launches public consultation on review of competition rules for distribution sector’ (28th July 2009) Brussels IP/09/1197. See also above, n.11 at p109

³⁸⁹ Press Release, ‘Antitrust: Commission launches public consultation on review of competition rules for distribution sector’ (28th July 2009) Brussels IP/09/1197 at p1

³⁹⁰ OJ (2010) L102/1

³⁹¹ Article 10 Regulation 330/2010. The Regulation is set to expire on 31 May 2022.

³⁹² European Commission, *Guidelines on Vertical Restraints* (2010) OJ C130/1

³⁹³ Above, n.338 at p650

³⁹⁴ The provisions regarding internet sales are not considered here due to their reduced relevance for beer supply agreements.

³⁹⁵ Above, n.338 at p660

fair share of the resulting benefits. However Recital 9 provides that where the market share thresholds are breached there is no such presumption.³⁹⁶ Equally, it provides where the market share thresholds are breached, there is no presumption of illegality under Article 101 TFEU. Further, Article 3(2) deals with multiparty agreements. It states that where an undertaking buys the contract goods or services from one undertaking party to the agreement and sells them to another undertaking party to the agreement, the market share of the first undertaking must respect the market share threshold of Article 3(1) as both a buyer and a supplier. Therefore should there be three parties to an agreement, all operating at a different level of trade, each party's market share must be below the 30% threshold in order for exemption to be possible.³⁹⁷

Through the implementation of these new market share thresholds the Commission has confirmed it remains wedded to this approach, notwithstanding the concerns discussed above regarding the adequacy of the 30% threshold. As noted by Colino, this extension in their use to both the buyer and the supplier had the potential to further 'aggravate' those concerns.³⁹⁸

3.2.2 Reaction to new market share criterion

The beer industry was not welcoming of the Commission's decision to impose the need to consider the buyer and the supplier's market share under Article 3 of the new BER. The British Beer and Pub Association (BBPA)³⁹⁹ highlighted the variety of agreements relied on in the UK pub sector and also emphasised the difficulty that would be experienced in assessing the market share of those undertakings operating in downstream markets.⁴⁰⁰ Similarly, the Brewers of Europe⁴⁰¹ expressed their concerns over the new market share requirements. Due to the significant differences in existing agreements, they stated that depending on the country and the size of the producer, this may have an important effect on the delivery contracts in place and cause significant uncertainty for producers, noting

³⁹⁶ Recital 9 Regulation 330/2010 and above, n.338 at p660

³⁹⁷ Above, n.392 at para 90, p20

³⁹⁸ Above, n.11 at p109

³⁹⁹ Hereinafter referred to as BBPA. This is an organisation representing brewing companies and their pub interests and pubcos in the UK.

⁴⁰⁰ BBPA, 'Response to the European Commission review of the competition rules applicable to vertical agreements' at p1 (*Europa*, October 2009)

<http://ec.europa.eu/competition/consultations/2009_vertical_agreements/britishbeerpubassoc_en.pdf> accessed 19th February 2015

⁴⁰¹ The voice of the European brewing sector

that it may be impossible for them to assess the market share of others with certainty.⁴⁰² Consequently there were common concerns that the new market share thresholds would narrow the scope of the BER and cause legal uncertainty.

3.2.3 Maintenance of the status quo for beer supply agreements

While Article 3 of Regulation 330/2010 implemented the Commission's desire for both the buyer's and supplier's market share to be subject to a cap, contrary to the wishes of some interested parties, this was largely the only departure from the regime under Regulation 2790/99. Therefore in keeping with the old regime, Article 5(1) of Regulation 330/2010 denied exemption to any direct or indirect non-compete obligation the duration of which was indefinite or exceeded 5 years. However, Article 5(2) echoed the terms of Regulation 2790/99. It stated that the five-year time limitation on non-compete obligations under Article 5(1) shall not apply where the contract goods or services are sold by the buyer from premises and land owned by the supplier or leased by the supplier from unconnected third parties and the duration of the non-compete obligation does not exceed the period of occupancy of the premises or land. Regulation 330/2010 has therefore again retained the deference of the past towards beer supply agreements where the premises are provided to the reseller.

In light of the maintenance of the foregoing concession, notwithstanding their concerns over the extended market share criterion, the BBPA, generally welcomed the new Regulation and Guidelines. However, the Campaign for Real Ale (CAMRA)⁴⁰³ and the Fair Pint campaign⁴⁰⁴ greatly opposed the renewal of the exemption for beer supply agreements. They objected to the Commission's assertion that due to the generally positive experience under Regulation 2790/99 it was appropriate to adopt a new BER.⁴⁰⁵ They expressed the view that the application of the BER in the UK market had not been positive. They highlighted that exemption of exclusive purchasing agreements and non-compete obligations had caused "*inflated prices, reduced competition and reduced amenity*".⁴⁰⁶ The Fair Pint Campaign submitted that exempted beer supply agreements, which at that

⁴⁰² The Brewers of Europe, 'Response to the European Commission review of the competition rules applicable to vertical agreements' (*Europa*, 28 September 2009)

<http://ec.europa.eu/competition/consultations/2009_vertical_agreements/thebrewersofeurope_en.pdf> accessed 29th June 2015

⁴⁰³ An independent consumer organisation which campaigns for real ale, pubs and consumer rights

⁴⁰⁴ A coalition of independent and tied landlords with the aim of removing the beer tie from all leased pubs

⁴⁰⁵ Campaign for Real Ale, 'European Commission review of the competition rules applicable to vertical agreements a response from CAMRA, The Campaign for Real Ale' at para 1.2, p2 (*Europa*, September 2009) <http://ec.europa.eu/competition/consultations/2009_vertical_agreements/campaignforrealale_en.pdf> accessed 19th February 2015

⁴⁰⁶ *Ibid* at para 1.2, p2

time tied more than 54% of the UK's public house market, had a significant effect on restricting competition. Amongst others, they foreclosed the UK market to competitors, increased prices and reduced consumer choice.⁴⁰⁷ This was deemed to be possible as no single company operating on the UK market had a market share in excess of 30% of the relevant market.⁴⁰⁸ The majority of UK pub companies had market shares of less than 5%.⁴⁰⁹ In order to address this situation, the Fair Pint Campaign had proposed that the Commission reduce the 30% market share threshold for exemption under the BER and that the *de minimis* threshold should also be reduced below a market share of 5% of the relevant market.⁴¹⁰ Despite these submissions, as noted above, the Commission opted to extend the 30% market share threshold until 31 May 2022.

4. Conclusion

Having charted above the evolution of the EU's approach to vertical agreements generally, it is apparent that they were initially treated defensibly by the Commission, on account of their 'double nature'. This approach was also bolstered by the goals of EU competition law, and most notably the integration objective. However, it has been shown that over the decades there have been swings in the treatment of vertical agreements in line with changing schools of thought and social and political environments. This gradual tolerance has resulted in most vertical agreements benefitting from exemption under the prevailing BER or obtaining individual exception under Article 101(3) TFEU.

With specific reference to beer supply agreements, as first distinguished in Regulation 1984/83, it has become apparent from this consideration of the evolution of the EU's approach toward such agreements that the Commission's practices have highlighted what Evereste has describes as a 'special deference'⁴¹¹ towards these. This has been despite the potential for such exclusive purchasing obligations to partition and foreclose markets, contrary to the goals of EU competition law. These widely recognised concerns have prompted the terms of successive BERs including the formalistic provisions of Regulation 1984/83 and the current economics-based Regulation 330/2010, to seek to limit the potentially harmful effects of such vertical restraints by restricting their scope and duration. Nevertheless, this general approach has long been caveated. The time-limits

⁴⁰⁷ Fair Pint Campaign, 'Review of the competition rules applicable to vertical agreements: a response from the Fair Pint Campaign' at para 2.8, p3 (*Europa*, September 2009)

<http://ec.europa.eu/competition/consultations/2009_vertical_agreements/fairpint_en.pdf> accessed 19th February 2015

⁴⁰⁸ Ibid at para 2.8, p3

⁴⁰⁹ Ibid at para 2.8, p3

⁴¹⁰ Ibid at para 2.9, p3

⁴¹¹ Above, n.121 at 610

imposed on all vertical agreements are inapplicable to beer supply agreements where the contract goods or services are sold by the buyer from premises and land owned by the supplier or leased by them from third parties. This leniency afforded by the various BERs towards such beer supply agreements has been supplemented, in particular, by the decisional practices of the European Commission, which often resisted attempts by the CJEU to adopt a more reasoned and economics-based stance towards such agreements. This was especially evident prior to the adoption of Regulation 2790/99, when Regulation 17/62 effectively ensured the Commission's monopoly in the application of Article 101(3) TFEU. However, as has been shown above, this was not confined to this period. The Commission appears to have developed a 'special deference' towards beer agreements from a relatively early stage, with this being evident through the decades, up to, and including, the current day Regulation 330/2010.

Through the implementation of Regulation 330/2010 the Commission has opted to largely maintain the *status quo* regarding the EU's acceptance of beer supply agreements. This is despite the concerns raised during the consultation process over the competitive implications of exempting tying agreements in the UK beer market. It is therefore instructive to consider in the next chapter the UK Government's policy on the regulation of the beer industry.

Chapter 4 - The United Kingdom Government's Policy on the Regulation of the Brewing Industry

The preceding chapter examined the application of the EU competition rules to vertical agreements with particular emphasis placed on those for the distribution of beer. In doing so it provided a contextual background to the EU's evolving approach towards beer tying agreements, which are now fully accepted by the EU as being a legitimate business model. This chapter now considers the UK's policy on the regulation of beer tying agreements following the decision in 2000 to revoke the Beer Orders and in doing so provides an overview of the development of the UK's approach towards these agreements and the influence the EU has had on the UK's tolerance of such arrangements.

The chapter first considers briefly the UK's accession to the EU and the challenges this presented to the UK courts in applying the EU competition law provisions in the context of beer tying agreements. The UK's refusal to award damages to tied tenants for breaches of Article 101 Treaty on the Functioning of the European Union (TFEU) is also considered (Subsection 1). The chapter then reviews the harmonisation of the UK and EU legal regimes applicable to vertical agreements such as beer tying agreements (Subsection 2). The on-going concerns and inquiries into the operation of the tied business model following the OFT's 2000 decision to revoke the Beer Orders are then addressed noting, amongst others, the Trade and Industry Committee and the Business Innovation and Skills Committee's heightened concerns over the operation of the UK market and the Office of Fair Trading's reluctance to intervene (Subsection 3). The Chapter then focuses on the Government's continued inaction on the matter of the beer tie (Subsection 4). The Government's policy change in light of past regulatory failings is then reviewed (Subsection 5). Finally the chapter considers the relevant provisions of the Small Business, Enterprise and Employment Act 2015 and the impact this will likely have on the UK beer market (Subsection 6).

1. EU Membership and its challenges for the UK courts

1.1 Implications of accession to the EU

The treatment of beer tie agreements in the UK has been influenced by the UK's accession to the EU in 1972. The relationship between national and EU law became subject to

various governing constitutional principles, most notably the supremacy of EU law.¹ This is applicable to the EU competition law provisions discussed in Chapter 3 and so came to impact on the handling of beer tie agreements in the UK. Following accession Regulation 67/67 granted all qualifying exclusive purchasing agreements, including beer tie agreements, an exemption from the prohibition of Article 101(1) TFEU.² This was due to their perceived benefits including improved distribution, which was of importance to the EU's unique integration agenda at that time.³ This offer of exemption remained under Regulation 1984/83⁴ and continues today under Regulation 330/2010.⁵

At the time of the UK's accession, it was significant that the EU was satisfied that the beer tie merited the possibility of block exemption given that the European Commission enjoyed sole authority to grant exemptions from Article 101(1) TFEU.⁶ However, the requirement for the national courts to apply Article 101(1) in conjunction with the Commission proved problematic for the UK courts as illustrated in *Holleran and Evans v. Thwaites plc*.⁷ There the exclusive supply obligation in the tenant's beer supply agreement made reference to broad categories of beer, not brands, which as discussed in Chapter 3 was a requirement of Article 6 of Regulation 1984/83.⁸ The English High Court accepted that this did not satisfy the requirements of the Regulation,⁹ however the European Commission had been involved in the case at a preliminary stage following a written complaint concerning the agreement.¹⁰ It subsequently notified Thwaites that certain clauses were out with the terms of the Regulation and negotiated with them to reach a conclusion on this without issuing a formal decision.¹¹ When reference was made to the Commission's refusal to make an interim decision, the High Court considered this to be

¹ Where a conflict between national and European law arises, EU law takes precedence. See Case 6/24 *Costa v. ENEL* [1964] ECR 585. See also R Whish and D Bailey, *Competition Law* 7th Edition (Oxford, Oxford University Press, 2012) at p75. In Case 14/68 *Walt Wilhelm v. Bundeskartellamt* [1969] ECR 1, it was confirmed that the principle of supremacy would be used to resolve any conflict between community and domestic law. In the UK the principle of supremacy was given effect by s.2(1) and s.3(1) of the European Communities Act 1972 on accession to the EU. Today the matter has been clarified by Article 3 of Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L1/1) which addresses the relationship between Articles 101 and 102 TFEU and national law.

² Commission Regulation (EEC) No 67/67 of 22 March 1976 on the application of Article 85(3) of the Treaty to certain categories of exclusive dealing agreements ([1967] OJ (spec ed) 10). See Chapter 3 for discussion.

³ *Ibid* at Recital 6

⁴ Commission Regulation (EEC) 1984/83 of 22 June 1983 on the application of Article 85(3) of the Treaty to categories of exclusive purchasing agreements ((1983) OJ L173/5)

⁵ Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices ((2010) OJ L102/1) Chapter 3, p100

⁶ Chapter 3, p58

⁷ *Holleran and Evans v. Thwaites plc* [1989] 2 CMLR 917

⁸ *Ibid* at 917 and Chapter 3, p68

⁹ Above, n.7 at 918

¹⁰ *Ibid* at para 16, p921

¹¹ *Ibid* at para 20, p922

“...no more than a factor to be taken into account...given that Article [101] has direct effect and so can be relied on in the national courts”.¹² As MacCulloch rightly highlights the national court’s dismissal of the Commission’s opinion, demonstrated the difficulties at that time between the national courts and the Commission’s procedures for enforcement of the EU competition law provisions.¹³

In order to encourage an efficient system for enforcing the EU competition law rules before national courts, the Commission drafted a Co-operation Notice setting out the policy on their application by the national courts.¹⁴ The Notice came into effect in 1993, the year after the compliance date for the Beer Orders. By that time, the effects of the Beer Orders on the UK market were becoming clear. Amidst the litigation in the UK regarding the price differential of beer sold to tied and free-of-tie tenants and concerns that the UK beer tie was incompatible with EU law discussed in Chapter 3, several cases disputing the legality under Article 101(1) TFEU of the tying provision of the pubco *Inntrepreneur Estates Limited*’s (IEL) lease were brought before the English courts.¹⁵ IEL had however notified their lease to the Commission with a view to obtaining negative clearance or individual exemption under Regulation 1984/83.¹⁶ In the cases before the UK courts, slow use was made of the 1993 Notice, as exemplified by *Inntrepreneur v. Mason*.¹⁷ The Commission had issued comfort letters in respect of IEL’s lease,¹⁸ stating that the conditions for individual retroactive exemption under Article 101(3) TFEU appeared to have been met and that retroactive exemption was proposed.¹⁹ The High Court however had difficulty following and applying the EU competition law provisions despite the guidance offered by the 1993 Notice.²⁰ The Court highlighted its discomfort in estimating the likelihood of exemption being granted, as required under its terms, despite the Commission twice making clear its intention do so through the aforementioned letters. The

¹² Ibid at para 66, p931

¹³ A MacCulloch, ‘Case Comment *Inntrepreneur Estates*: Co-operative application of the EC competition rules in the United Kingdom?’ (1995) 16(6) E.C.L.Rev 380 at 381

¹⁴ European Commission, *Notice on cooperation between national courts and the Commission in applying Articles 85 and 86 of the EEC Treaty* ((1993) OJ C39/6) (the 1993 Notice). Also, ibid at 380

¹⁵ For example *Inntrepreneur Estates Ltd v. Mason* [1993] 2 CMLR 293; *Inntrepreneur Estates (GL) Ltd v. Boyes* [1995] E.C.C. 16; *Inntrepreneur Estates (CPC) Ltd v Bayliss* [1998] Eu LR 483. These cases involved challenges before the English Courts to the tying provisions in IEL’s lease which tenants alleged were contrary to Article 101(1) TFEU. Also above, n.13 at 381.

¹⁶ Chapter 3, p84

¹⁷ *Inntrepreneur Estates Ltd v. Mason* [1993] 2 CMLR 293

¹⁸ Prior to the adoption of Regulation 1/2003 the Commission often granted exemptions through comfort letters rather than formal decisions. D.G. Goyder *EC Competition Law* 3rd Edition (Oxford, Oxford University Press, 1998) at p128. See also *Inntrepreneur Estates Ltd v. Mason* [1993] 2 CMLR 293 at para 38-39, p303-304. When the Masons, assignees of a lease of a tied public house, fell into arrears and IEL sought to forfeit the lease and claim relief, the Masons subsequently claimed the lease was void as it failed to come within the terms of Regulation 1984/84.

¹⁹ Above, n.17 at para 38-39, p303-304

²⁰ Above, n.13 at 382

High Court's difficulty stemmed from the fact that although the letters indicated the Commission's intention to exempt the lease, they were not deemed to be 'comfort letters' within the meaning of the 1993 Notice.²¹ However, as MacCulloch notes, the High Court did not seek any guidance from the Commission or stay proceedings in order to give the Commission the opportunity to commence the exemption procedure.²² This approach was nevertheless approved by the UK Court of Appeal in *Boyes*,²³ although greater co-operation was apparent in *Bayliss*.²⁴ There the High Court was prepared to hold off enforcing the tying provision under an IEL lease until the Commission had decided whether to grant individual exemption under Article 101(3) TFEU.²⁵ There was therefore some acceptance by the national court that the conclusion of the Commission's procedure was central to the decision at the national level.²⁶

1.2 The UK's refusal to award damages to tied tenants for breaches of Article 101 TFEU

Challenges to beer supply agreements also came before the UK courts in light of developments in EU case law in the 1990s, which established that in certain circumstances national courts should award damages to private litigants who suffer as a result of a Member States' breaches of EU obligations.²⁷ However, it remained to be clarified whether it was possible to claim for a breach of the EU competition provisions where financial loss resulted from such a breach by a third party, rather than by a Member State.²⁸ The UK courts however refused to depart from the national legal principle of *in pari delicto*. This prevented the parties to an illegal contract relying on that illegality as a basis for a claim for damages from a co-contractor, regardless of whether they benefitted from bargaining power or were forced into acceptance of an arduous contract.²⁹

²¹ Above, n.17 at p294 and para 43-44, p305

²² Above, n.13 at 382 and 1993 Notice at para 30, p9

²³ *Inntrepreneur Estates (GL) Ltd v. Boyes* [1995] ECC 16. This concerned an action for the recovery of possession of a tied house. The main question of law was whether the tying provision under the IEL lease was contrary to Article 101 TFEU. With regard to the *Mason* case, the Court stated "[t]his judgment has provided welcome assistance on the hearing of this appeal." (at para 7, p18)

²⁴ *Inntrepreneur Estates (CPC) Ltd v Bayliss* [1998] Eu LR 483

²⁵ The Court refused to determine whether or not an injunction to enforce the terms of the tying agreement should be granted until the Commission had ruled on the matter, noting that it would be inappropriate for the national court to do so as the matter came within the Commission's exclusive jurisdiction. (Ibid at p483-484)

²⁶ Above, n.13 at 383

²⁷ For example C-6 and 9/90 *Francovich v. Italy* [1991] ECR I-5357 and Case 46-93 *Brasserie du Pêcheur SA v. Germany* [1996] ECR I-1029. D.G. Goyder, *EC Competition Law* 4th Edition (Oxford, Oxford University Press, 2003) at p466 and R Whish, *Competition Law* 6th Edition (London, Oxford University Press, 2009) at p232

²⁸ D.G. Goyder, *EC Competition Law* 4th Edition (Oxford, Oxford University Press, 2003) at p466-467

²⁹ Ibid at p467

The application of this principle was demonstrated in the Court of Appeal's decision in *Gibbs Mew v. Gemmell*.³⁰ The tenant Gemmell was in rent arrears and was sued by his landlord, Gibbs Mew, a small brewer. The tying provisions of the lease referred to beers by type not brand.³¹ Gemmell subsequently claimed that Regulation 1984/83 was inapplicable, and counterclaimed for damages in restitution of the sums he had paid for beer under the contract. While the agreement was *de minimis*, the Court of Appeal still considered the matter.³² Whilst it was considered that the agreement did not breach Article 101(1) TFEU, however the Court considered the remedies available to the tenant for such a breach including their right to claim damages for an infringement of the Treaty provision.³³ It stated that whilst Article 101 TFEU was directly effective, it was intended to protect third party competitors not the parties to a beer tie agreement that offends Article 101 TFEU.³⁴ It was accepted that the parties to the offending agreement were the cause rather than the victims of the distortion, restriction or prevention of competition.³⁵ Applying national law, and so the principle of *in pari delicto*, the English Court refused to allow tenants to claim for damages on the basis that their lease, incorporating the beer tie, infringed Article 101 TFEU with this judgment being followed later that year in *Crehan*.³⁶

Crehan was a tenant under a long lease with Innpreneur.³⁷ When an action was brought for arrears for beer supplied, *Crehan* defended this and counterclaimed that the beer tie breached Article 101(1) TFEU as it prevented him from purchasing beer on the open market from the cheapest sources, and also foreclosed the outlets available to competing suppliers' beers.³⁸ Following the Court of Appeal in *Gemmell*, the counterclaim was dismissed on the basis of the principle of *in pari delicto*.³⁹ This case however went on to have a long passage through the European and UK Courts and further illustrated the difficulties the UK courts experienced in applying the EU competition law provisions in tandem with the Commission. Under a preliminary reference from the Court of Appeal, in addressing the question of whether a party to a prohibited tied house agreement could rely on Article 101 TFEU in order to seek relief from the other party, the Court of Justice of the

³⁰ *Gibbs Mew v. Gemmell* [1998] Eu LR 588

³¹ *Ibid* at 601. This case was heard by the English Court of Appeal just prior to the European Commission's notice of its acceptance of the UK formulation of the beer tie based on tying by type rather than brand, as discussed in Chapter 3.

³² Above, n.30. Also J.M. Walker, 'Have English Courts gone too far in challenging the effectiveness of EC Competition Law?' (1999) 20(1) ECL Rev 1 at p2-3

³³ Above, n.30 at p603-604

³⁴ *Ibid* at p604-605

³⁵ *Ibid* at p604

³⁶ *Courage Limited v. Crehan (No.1)* [1999] Eu LR 409

³⁷ *Ibid* at 409

³⁸ *Ibid* at 410

³⁹ *Ibid* at 410

European Union (CJEU) established that the party could do so, thereby countering the English rule of *in pari delicto*.⁴⁰ The CJEU however stated that regard had to be had to the EU recognised principle that it should not be possible for a litigant to profit from his own unlawful conduct, with EU law allowing national rules to prohibit this where that party bore significant responsibility for the distortion of competition.⁴¹ In determining the party's degree of responsibility, the national court was to have regard to the parties' respective bargaining power and conduct.⁴² Consequently, as noted by Cumming the CJEU sought to protect the practical effect of Article 101 TFEU and to ensure effective protection for rights under the Treaty.⁴³ By allowing a contracting party to an agreement that infringes Article 101 TFEU to claim damages, the CJEU contributed to the use of national courts in the enforcement of Article 101 TFEU.⁴⁴

Following the preliminary reference however, in 2003 the High Court heard Crehan's claim.⁴⁵ While it was accepted that Crehan would have been entitled to damages had his lease infringed Article 101(1) TFEU, the first *Delimitis* condition of foreclosure was not deemed to be satisfied by the UK beer market.⁴⁶ Nevertheless, this was later reconsidered by the English Court of Appeal and damages were awarded.⁴⁷ It was noted that the European Commission had investigated the relevant market on numerous occasions and, when considering the Inntrepreneur leases had found Article 101(1) TFEU was applicable to these during the relevant period.⁴⁸ The Court had erred by concluding that the Commission was wrong in doing so with this creating inconsistency in the application of the EU competition law provisions.⁴⁹ Nevertheless, Inntrepreneur ultimately successfully appealed the decision to the UK Supreme Court.⁵⁰ There it was opined that it was for the English court to determine whether or not Article 101(1) TFEU was applicable and it had properly reached its own conclusion in assessing the evidence before it.⁵¹ The Supreme Court clarified that where a judge concludes that a decision of the Commission is incorrect it would be inconsistent with their judicial oath to nevertheless follow that decision.⁵² Crehan therefore failed to recover any damages in respect of his beer tie agreement with

⁴⁰ Case C-453/99 *Courage Ltd v. Crehan* [2002] QB 507 at 507-508

⁴¹ *Ibid* at 507-508

⁴² *Ibid* at 508

⁴³ G.A. Cumming, 'Case Comment *Courage Ltd v Crehan*' (2002) 23(4) ECL Rev 199 at 199

⁴⁴ *Ibid* at 201

⁴⁵ *Crehan v Inntrepreneur Pub Company (CPC), Brewman Group Limited* [2004] E.C.C. 8 at H7 p79-80

⁴⁶ Above, n.40 at H11, p80-81

⁴⁷ *Crehan v. Inntrepreneur Pub Co CPC*, [2004] EWCA Civ 637

⁴⁸ *Ibid* at para 1, p 804 and see Chapter 3 for discussion on the Inntrepreneur leases.

⁴⁹ Above, n.47 at para 1, p 804

⁵⁰ *Crehan v. Inntrepreneur Pub Co (CPC) and another (Office of Fair Trading and other intervening)* [2007] 1 AC 333

⁵¹ *Ibid* at p334

⁵² *Ibid* at para 69, p356-357

this setting-back the private enforcement of the EU competition provisions for UK tied tenants.

The position of the tied tenant in the UK was however further complicated following the Court of Appeal's decision in *Passmore v. Morland*.⁵³ There it stated that as Article 101 TFEU is essentially an effects based prohibition applying to agreements and concerted practices which have an offensive economic objective or effect, it becomes inapplicable when the circumstances change.⁵⁴ Therefore when a tenancy agreement was assigned from Innentrepreneur, one of the largest pubcos in operation, to Morland, a small brewery,⁵⁵ the Court of Appeal held that even if the agreement with Innentrepreneur breached Article 101 TFEU, on assignment, the prohibition no longer applied. The effects of the agreement changed due to the far smaller degree of market power enjoyed by Morland.⁵⁶ Consequently, the Court of Appeal took the view that not only is the prohibition imposed by Article 101(1) TFEU 'temporary or transient' in effect but so too is the sanction of nullity under Article 101(2) TFEU.⁵⁷ Whilst this was a positive outcome in the sense of potentially preserving the legality of commercial agreements between parties, it also increased doubt over the availability in the UK of a remedy for disgruntled tied tenants.

2. Harmonisation of the UK and EU legal regimes applicable to beer tying agreements

In light of the foregoing, for several years after accession to the EU the UK courts and businesses appeared to grapple with the application of the European competition law provisions and the availability of remedies for their breach. At one point an estimated 800 beer supply agreements awaited decision in the English courts largely due to the legal uncertainty surrounding the application of the competition law rules to them.⁵⁸ Whilst the jurisdiction of the EU competition law provisions was limited by the requirement that the conduct in question have an 'effect on trade between Member States' and although this had been broadly interpreted, there were many circumstances in which domestic competition law applied to the beer tie agreement in issue. Consequently, during the 1990s, as Europe

⁵³ *David John Passmore v Morland and Others* [1999] 3 All ER 1005; [1999] 1 CMLR 1129; 1 Eur LR 501

⁵⁴ *David John Passmore v Morland and Others* [1999] 1 CMLR 1129 at para 25 and 26, p1139-1140. See also D.G. Goyder, *EC Competition Law* 4th Edition (Oxford, Oxford University Press, 2003) at p468

⁵⁵ *David John Passmore v Morland and Others* [1999] 1 CMLR 1129 at para 11, p1134

⁵⁶ *Ibid* at para 25-27, p1139-1141. D.G. Goyder, *EC Competition Law* 4th Edition (Oxford, Oxford University Press, 2003) at p468

⁵⁷ *Above*, n.55 at para 55, p1150

⁵⁸ D Cowan and J Nazerali, 'Beer Supply Agreements – a Step Forward or Last Orders?' (1998) 19(5) E.C.L.Rev 289 at p294

was actively considering vertical restraints reform,⁵⁹ the UK broke away from its past, enacting the Competition Act 1998 and the Enterprise Act 2002.⁶⁰ It was however made clear “... *that the purpose...is to ensure as far as possible a consistency with E[U] approach and thereby ease burdens for business.*”⁶¹

2.1 Chapter I Prohibition

The Competition Act 1998 (1998 Act) is now the principal statute in UK competition law and policy with the main provisions coming into force on 1 March 2000. This introduced new rules known as the Chapter I and Chapter II prohibitions. The Chapter I prohibition is contained in s.2 of the 1998 Act and is modelled very closely on Article 101(1) TFEU. As such, it states

“(1) Subject to section 3,⁶² agreements between undertakings, decisions by associations of undertakings or concerted practices which-
(a) may affect trade within the United Kingdom, and
(b) have as their object or effect the prevention, restriction or distortion of competition within the United Kingdom,
are prohibited unless they are exempt in accordance with the provisions of this Part.”

Section 18 of the 1998 Act contains the Chapter II prohibition which is closely modelled on Article 102 TFEU and as such forbids the abuse of a dominant position.⁶³ In line with the intention to harmonise national and EU law, s.60 of the 1998 Act states the principles to be applied in determining questions in relation to competition within the UK, and requires where possible, that there should be consistency with the treatment of corresponding questions arising under EU law.⁶⁴ It therefore requires close conformity between the 1998 Act and the EU competition law regime, to the extent that is relevant in a national context. Conformity is also ensured by s.10 of the 1998 Act which provides for parallel exemptions, stating that an agreement is exempt from the Chapter I prohibition if it

⁵⁹ Chapter 3, p88

⁶⁰ This essentially implemented other changes to UK competition law, including, a new system of market investigations and merger control. This will not be discussed further. The Restrictive Trade Practices Act 1976 and the Fair Trading Act 1976 were repealed.

⁶¹ Lord Haskel, HL Deb 17th November 1997, col 417

<<http://www.publications.parliament.uk/pa/ld199798/ldhansrd/vo971117/text/71117-18.htm>> accessed 1st May 2015. As Furze highlights this approach was adopted when there was no obligation on Member States to align their laws with those of the EU. (M Furze, *Competition law of the EC and UK* 6th Edition (Oxford, Oxford University Press, 2008) at p55) The focus here shall be the Competition Act 1998 and the Chapter I prohibition.

⁶² Section 2(3) of the 1998 Act states that section 2(1) is only applicable “*if the agreement, decision or practice is, or is intended to be, implemented in the United Kingdom*”.

⁶³ This will not be discussed further

⁶⁴ Section 60(1) 1998 Act

is exempt from the Community prohibition by virtue of, amongst others, a Regulation. Section 10(2) of the 1998 Act states that this is so even where the agreement does not have the necessary effect on trade between Member States, as required for the application of Article 101(1) TFEU, but falls within a category of agreements which is exempt under a Regulation. Section 10 therefore wholly imports all EU block exemptions into UK national law.

2.2 Vertical agreements and the Chapter I Prohibition

The s.60 requirements are however open to limitation in that, for example, judgments of the European Courts that are motivated by single market considerations may not be followed by the UK courts.⁶⁵ Further, the application of the Chapter I prohibition to vertical agreements, such as beer supply agreements, was extensively debated.⁶⁶ As discussed in Chapter 3, the European Court had established that Article 101(1) TFEU was applicable to vertical agreements, however the UK authorities decided that as EU policy was largely influenced by single market considerations and in particular their unique goal of market integration, it should adopt its own distinctive approach to vertical restraints.⁶⁷ This decision was also influenced by the desire to reduce the number of precautionary notifications to the UK competition authorities of agreements which were not anticompetitive.⁶⁸ As a result, by virtue of s.50 of the 1998 Act, the Secretary of State excluded vertical agreements from the Chapter I prohibition.⁶⁹ However, this would later

⁶⁵ Section 60(1) of the 1998 Act states that the requirement applies “*in so far as is possible (having regard to any relevant differences between the provisions concerned)*”. For example, s.2(1)(a) of the 1998 Act provides that the Chapter I Prohibition only applies where “*trade is affected within the United Kingdom*” and so departs from the EU test of an effect on interstate trade which is linked to the market integration goal. K Middleton, ‘Harmonisation with community law: the Euro clause’ in B Rodger and A MacCulloch, eds, *The UK Competition Act, A new era for UK competition law* (Oxford, Oxford, Hart Publishing, 2000) at p26 and p28, and R Whish and D Bailey, *Competition Law* 7th Edition (Oxford, Oxford University Press 2012) at p59

⁶⁶ R Whish, ‘The Competition Act 1998 and the prior debate on reform’ in B Rodger and A MacCulloch, eds, *The UK Competition Act, A new era for UK competition law* (Oxford, Hart Publishing, 2000) at p13-14

⁶⁷ B Rodger and A MacCulloch, *Competition Law and Policy in the EC and UK* 3rd Edition (London, Cavendish Publishing, 2004) at p199-200

⁶⁸ Department of Trade and Industry, *Competition Act 1998 Exclusion of Vertical Agreements Consultation on a draft Order* (4th February 1999) at para 6

⁶⁹ Section 50 of the 1998 Act entitled the Secretary of State to make an order to provide for exclusions or exemptions or otherwise for prescribed provisions not to apply in relation to vertical or land agreements. As a result, The Competition Act 1998 (Land and Vertical Agreements Exclusion) Order 2000 SI 2000/310 was enacted and Article 3 excluded all vertical agreements from the Chapter I Prohibition with the exception of those imposing minimum or fixed resale prices (Article 4 SI 2000/310). Article 2 of the Order also excluded agreements to the extent that they constituted a ‘land agreement’. Beer tie agreements could therefore potentially benefit from both the Article 2 and the Article 3 exclusions with different parts of the agreement benefitting from different exclusions. This was effective from March 2000 until 30th April 2005. B Rodger and A MacCulloch, ‘The Chapter I Prohibition: Prohibiting cartels or permitting verticals? Or both?’ in B Rodger and A MacCulloch, eds, *The UK Competition Act, A new era for UK competition law* (Oxford, Hart Publishing 2000) at p189-190

change with the adoption of Regulation 1/2003.⁷⁰ Following its implementation the European Commission now shares competence in applying Articles 101 TFEU in its entirety, with National Competition Authorities and Courts making it preferable for the UK to align its domestic law on vertical agreements with that of the EU.⁷¹ A review of the UK's vertical restraint policy subsequently culminated in the adoption of an Order to repeal the exclusion of vertical agreements from the Chapter I prohibition.⁷² In keeping with the Government's earlier expressed intention to rely on parallel exemptions stemming from Regulation 2790/99 then in force,⁷³ it subsequently extended the application of the Regulation to all vertical agreements, either directly or indirectly, where there was no effect on inter-state trade only in the UK. In doing so it completed the radical Europeanisation of UK law on vertical agreements, including beer supply agreements.

3. Continued concerns and inquiries in the UK market following the OFT's decision to revoke the Beer Orders

Consequently, in 2000, two significant events occurred. The 1998 Act came into force and as discussed in Chapter 2, the OFT deemed the UK market sufficiently competitive for the Beer Orders to be revoked. Nevertheless concerns over the level and impact of the concentration of public house ownership in the UK and the extensive use of beer tying agreements did not dissipate.

As discussed in Chapter 2, the Beer Orders had not been the most appropriate response to the issues faced in the UK beer market and as a result the aim of increasing competition within the brewing industry through their implementation failed to be achieved. They had several consequences that were largely unforeseen at the time of their implementation. As several brewers concluded that it would be desirable to specialise in either brewing or retailing, whilst others simply exited the brewing business, the market became

⁷⁰ Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L1/1. This replaced Regulation No 17 and the centralised scheme it established. This was deemed to hamper the application of the EU competition law provisions by national competition authorities and courts, whilst the system of notification prevented the Commission from focusing on the most serious infringements of the competition law provisions. (Recital 3 Regulation 1/2003) It therefore sought to establish a directly applicable exception system under which the national courts and authorities have the power to apply Article 101 TFEU in its entirety (Recital 4, Regulation 1/2003).

⁷¹ Department of Trade and Industry, *Government response to the consultations on giving effect to Regulation 1/2003 and aligning the Competition Act 1998 including exclusions and exemptions* (16th January 2004)

⁷² The Competition Act 1998 (Land Agreements Exclusion and Revocation) Order 2004 SI 2004/1260

⁷³ Department of Trade and Industry, *Productivity and Enterprise: A world class competition regime* (Cm 5233, 2001) at para 8.14-8.16. Above, n.67 at p200

exceptionally concentrated.⁷⁴ The divestiture of public houses in accordance with the terms of the Beer Orders also resulted in the growth of pubcos that, as discussed in Chapter 2, have perpetuated the tied house system and its associated competition concerns.

However, despite the ongoing interest that would subsequently be shown in the UK market following the revocation of the Beer Orders, prompting a significant level of reporting, no real change in the regulation of the UK market would be implemented over the coming decade. This was so even although the terms of many of these reports were damning for the industry and clearly indicated numerous on-going anticompetitive issues surrounding the operation of the beer tie. The unforeseen consequences of the Beer Orders discussed in Chapter 2 appeared to have a chilling effect with regard to further intervention in the market, with several of the reports produced noting the sponsoring organisation's reluctance to suggest far reaching or 'eye catching' recommendations.⁷⁵ Over this period the OFT also exhibited an on-going reticence to interfere in the market often citing the EU's acceptance of the beer tie in support of its position, with the Government tending to follow its lead with regard to proposed interventions. Nevertheless other bodies, most notable the Business Innovation and Skills Committee (BISC) and the pressure group the Campaign for Real Ale (CAMRA) were more persistent and activist in this regard. Further, not long after the OFT's decision to revoke the Beer Orders, in 2002 Federation of Small Businesses (FSB) requested the OFT investigate the market for the resale of beer through public houses.⁷⁶ This would be the precursor to numerous and on-going investigations into the UK market despite the fact the OFT declined to pursue the FSB's request. It defaulted

⁷⁴ M.E. Slade, 'Beer and the Tie: Did divestiture of Brewer Owned Public Houses Lead to Higher Beer Prices?' (1998) 108 *The Economic Journal* 565 at 573-574

⁷⁵ Business and Enterprise Committee, *Pub Companies* (HC 2008-2009, 26-1) at p4 and para 11, p8

⁷⁶ Their concerns were focused on how much tied tenants had to pay for beer; their level of rent; the inadequate support provided by pubcos; and that beer ties caused a restriction of choice which was anti-competitive. They asked the OFT whether the Chapter I or Chapter II prohibition of the 1998 Act had been breached by virtue of pubcos making anti-competitive agreements with their tenants; and if grounds existed to refer pubcos to the Competition Commission under the monopoly provisions of the Fair Trading Act 1973 which would soon be replaced by the market reference provisions of the Enterprise Act 2002. Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at para 29, p15 and Trade and Industry Committee, *Pub Companies Volume II* (HC 2004-2005, 128-II) at Appendix 22, Ev232

to the position that the beer tie did not infringe the EU competition provisions.⁷⁷ The OFT believed competition was working well and was not being prevented, restricted or distorted by pubcos, and so, refused to refer the matter to the Competition Commission.⁷⁸ However, despite the OFT's reluctance to investigate the market and due to the FSB's growing concerns over the concentration of public houses in the hands of large pubcos and their operation of the tied model, in 2004 the Trade and Industry Committee (TIC) investigated the matter.⁷⁹

3.1 The Trade and Industry Committee's Investigation

The Trade and Industry Committee (TIC) noted that on numerous occasions the European Commission and Courts have considered arrangements between national brewers and pubcos, and their respective tied tenants under Article 101 TFEU.⁸⁰ While, as discussed in Chapter 3 the old leases of the national brewers had been found to come within Article 101 TFEU, the TIC highlighted that the current leases underwriting pubco arrangements had not been found to infringe Article 101 TFEU.⁸¹ The TIC however addressed the definition of the final market for the consumption of beer noting that this was one of the principle areas of contention between tenants and competition authorities.⁸²

3.1.1 Market definition

As discussed in Chapter 3, the CJEU in *Delimits* considered the reference market to be that “for the distribution of beer in premises for the sale and consumption of drinks”.⁸³ However, the TIC noted that since the Beer Orders, the OFT have come to apply a stricter market definition ‘in tandem’ with that of the European Commission, defining it “both in

⁷⁷ Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at para 30, p15. The OFT clarified that it had to take into account the application of EU law to similar questions raised under it. It was noted that the European Commission and Courts have held that Article 101 TFEU is inapplicable to agreements between pubcos and their tenants where the pubcos acquire their drinks from a number of sources or are too small to contribute to the foreclosure of retail outlets to competitors. (See *Roberts and Roberts*, Chapter 3, p81 and Trade and Industry Committee, *Pub Companies Volume II*, (HC 2004-2005, 128-II) at Appendix 22, para 21, Ev234.) They also found no ground for withdrawing the benefit of the exclusion from the Chapter I Prohibition as the agreements between pubcos and their tenants came within the terms of the Competition Act (Land and Vertical Agreements Exclusion) Order 2000, then in force, as they involved the transfer of land rights, namely the public house. ((HC 2004-2005, 128-I) at para 30, p15). The refusal to do so was also deemed to be supported by the competitiveness of the on-trade sector and the danger that the OFT would take action that was inconsistent with the European Commission and Courts' approach. ((HC 2004-2005, 128-II at para 22, Ev234)

⁷⁸ Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at para 31, p15-16. In its 2000 Report *The Supply of Beer*, the OFT found that pubs were increasingly competing with other on-trade outlets including clubs, bars and increasingly restaurants. See Chapter 2.

⁷⁹ Trade and Industry Committee, *Pub Companies* (HC 2004-2005, 128-I) at p3

⁸⁰ *Ibid* at para 25, p13

⁸¹ *Ibid* at para 28, p13

⁸² Above, n.79 at para 32, p17

⁸³ Chapter 3, p78

terms of full on-licences and in terms of all on-licences”.⁸⁴ The FSB claimed that the pub sector constituted a distinct market in itself, although the OFT refused to accept this noting that although they had not been required to conduct in depth analysis of market definition, there were “*significant doubts about whether pubs are in a discrete market*”.⁸⁵ While the TIC acknowledged that there was an overlap between public houses and other outlets whose main purpose is selling alcohol for consumption on the premises, they questioned the OFT’s market definition as they considered that from the standpoint of the consumer, there is a distinction between going to a public house for a drink and going for a meal in premises where alcohol may be consumed.⁸⁶ Therefore, if the public house market was not a discrete market, all on-licensed premises did not constitute a ‘coherent market either’.⁸⁷ The TIC therefore correctly stated that the OFT should reconsider this in order to more accurately define the market and establish mechanisms for monitoring it.⁸⁸

However, under any of the possible market definitions considered, no pubco, brewer or retail pub chain was considered to hold a dominant position in the total market for beer.⁸⁹ At that time, Enterprise was the largest pubco in operation and owned 15% of all public houses, which were all tenanted and to whom it acted as wholesaler and had no brewing operations.⁹⁰ The TIC also stated their agreement with the OFT’s position that there are sufficient different types of public houses, namely managed, tenanted and free houses, for there to “*be a reasonable amount of competition between on-trade outlets*”.⁹¹ It did however acknowledge that there may be higher concentrations of public house ownership in certain regions or areas.⁹²

3.1.2 Wholesale supply, small brewers and distribution problems

The TIC considered wholesale supply of beer noting the MMC’s concerns in 1989 that this was largely controlled by the national brewers resulting in higher beer prices.⁹³ Today pubcos either have their own distribution networks or are supplied directly by brewers.⁹⁴ While the TIC established that no pubco had a dominant position in the wholesale market

⁸⁴ Above, n.79 at para 36, p18 and Monopolies and Mergers Commission, *The Supply of Beer A Report on the supply of beer for retail sale in the United Kingdom* (Cm 651, 1989) at para 2.128, p45

⁸⁵ Above, n.79 at para 36, p18

⁸⁶ Ibid at para 37, p18

⁸⁷ Ibid at para 37, p18

⁸⁸ Ibid at para 38, p18

⁸⁹ Ibid at para 18, p11

⁹⁰ Ibid at para 19, p11

⁹¹ Ibid at para 19, p11

⁹² Ibid at para 19, p11

⁹³ Ibid at para 42, p19 and Trade and Industry Committee, *Pub Companies Volume II* (HC 2004-2005, 128-II) at para 7, Ev 233

⁹⁴ Above, n.79 at para 44, p19

for beer,⁹⁵ they received evidence that tenants and consumers' access to locally brewed beers remained a concern as the beer tie along with pubcos' centralised distribution systems prohibited small brewers from supplying public houses in their area.⁹⁶ Small brewers experienced significant logistical issues in supplying pubcos. As pubcos often outsourced their distribution to international brewers' distribution arms, small brewers found it both impractical and prohibitively expensive to deliver their goods to brewer's regional warehouses which were significant distances from their breweries.⁹⁷ Although the Society of Independent Brewers' Association's (SIBA) Direct Delivery Scheme (DDS) assisted some small brewers in this regard,⁹⁸ their position was considered to have been worsened by the recent sale of one of the few independent wholesalers to the brewer Scottish Courage.⁹⁹ The big four international brewers dominated the market through their distribution systems and discounts, with SIBA submitting that this was encouraged by pubcos operating practices.¹⁰⁰ Various respondents suggested that the difficulties experienced by small brewers in accessing the market could be alleviated by reintroducing the Guest Beer provisions (GBP) of the Beer Orders,¹⁰¹ however, the TIC accepted that the reintroduction of a statutory GBP would run counter to EU competition law and cause the UK Government to be legally challenged.¹⁰² In contrast to the OFT's finding in 2000,¹⁰³ discussed in Chapter 2, the TIC however recognised the need for there to be greater consumer choice and recommended pubcos offer their tenants increased flexibility regarding the products they sell, thereby affording small brewers greater opportunity to participate in the market.¹⁰⁴ They also highlighted that the largest international brewers enjoyed a "*stranglehold on the distribution of beer*" on account of their distribution, rather than their supply contracts with pubcos¹⁰⁵ and concluded that there was a "*strong possibility of anti-competitive consequences*" in the distribution market for beer, prompting them to request the OFT keep it under close scrutiny.¹⁰⁶

⁹⁵ Ibid at para 46, p20

⁹⁶ Ibid at para 47, p20

⁹⁷ Ibid at para 62, p23-24

⁹⁸ The DDS acted as a 'middle person' between the brewers and the pubcos with pubco orders being sent to the brewers who delivered directly to the public houses where they were required. Above, n.79 at para 64, p23

⁹⁹ Above, n.79 at para 66, p23

¹⁰⁰ Ibid at para 48, p20

¹⁰¹ Ibid at para 55, p22

¹⁰² Ibid at para 61, p23. Chapter 2, footnote 264, p37

¹⁰³ Office of Fair Trading, *The Supply of Beer* (OFT 317, 2000)

¹⁰⁴ Above, n.79 at para 61, p23

¹⁰⁵ The largest brewers retained control of credit control, ordering and distribution when they sold their public houses in compliance with the Beer Orders. Ibid at para 67 and para 69, p25

¹⁰⁶ Above, n.79 at para 71, p25

3.1.3 The cost of the tie to tenants

The TIC also received evidence from many tenants who complained of excessive wholesale prices for tied products, which made them uncompetitive in their local markets.¹⁰⁷ The TIC established that whilst the wholesale selling price quoted to tied tenants was largely similar to the standard wholesale selling price at which free houses purchased beer, the actual wholesale price paid by pubco tenants was higher due to the discounts subsequently offered to free houses.¹⁰⁸ The TIC accepted that the terms of commercial contracts should remain confidential however they proposed that pubcos be more transparent regarding the discounts available to tied tenants compared to free house operators.¹⁰⁹ As the TIC's inquiry was initiated following complaints regarding inequality in the contractual relationship between pubcos and their tenants, the TIC attempted to balance the costs and benefits of the tie to tenants.¹¹⁰ In doing so it concluded that whilst the 'quantifiable costs of the tie were usually balanced by the benefits available to the tenants',¹¹¹ their analysis was an approximate guide "*backed by many assumptions, some of which we believe are unrealistic.*"¹¹² They noted that the costs and benefits are not equal in all cases, with some tenants finding themselves in financial hardship, suggesting that more could be done by pubcos to redress the imbalance.¹¹³

3.1.4 Ending the beer tie

In light of the foregoing concerns it was suggested that many of the issues faced by tenants could be resolved by removing the beer tie thereby freeing tenants to purchase beer on the open market.¹¹⁴ The TIC however concluded that it was not certain that doing so would improve the position of tenants. Pubcos being property companies would offset their loss of income from the wholesale price differential they charge by imposing higher rents on tenants as they would no longer have an interest in expanding the tenant's business.¹¹⁵ The TIC was also concerned that doing so would allow the national brewers to have a 'virtual monopoly' on the wholesaling of beer, as they did prior to the Beer Orders. As they already controlled the national distribution of beer through their ownership of the

¹⁰⁷ Ibid at para 112, p35

¹⁰⁸ Ibid at para 124, p38

¹⁰⁹ Ibid at para 125, p28

¹¹⁰ Ibid at para 188, p54

¹¹¹ Ibid at para 188, p54

¹¹² Ibid at para 179, p52

¹¹³ Ibid at para 188, p54

¹¹⁴ Ibid at para 189, p54

¹¹⁵ Ibid at para 198, p56

distribution companies that deliver to the majority of tenanted houses for the pubcos, removing the tie would be enable them to supply the free-of-tie tenants directly.¹¹⁶

3.1.5 Statutory code for pubcos

In light of the foregoing concerns numerous recommendations were made during the course of the inquiry to improve the relationship between the pubcos and their tenants, including a strengthened voluntary code of conduct. Given the fairly recent and significant interventions in the market via the Beer Orders, this was a relatively safe recommendation for the TIC to make. While the TIC refrained from requiring a legally binding code, it was clarified that if the industry failed to show signs of accepting and complying with an adequate voluntary code¹¹⁷ then “*the Government should not hesitate to impose a statutory code on it*”.¹¹⁸ The TIC therefore passed the responsibility for implementing more significant reform to the Government however given its response to the report this was highly unlikely to happen.

Despite the strong terms of the TIC’s report, dismissive responses to it were received from the OFT and the Government.¹¹⁹ The Government stated that it would have difficulty imposing a statutory code of practice which would prescribe the terms and conditions of commercial agreements.¹²⁰ It also stated that the competition concerns raised were for the competition authorities to deal with. The OFT was similarly dismissive of the report stating that it keeps the market definition for the beer sector under review; that it lacked any evidence of anti-competitive behaviours amongst distributors; and as no company holds a dominant position in the supply of beer the problems faced by tenants and small brewers were not a basis on which it could exercise its competition enforcement powers.¹²¹ The primary recommendation of an updated voluntary code of conduct was however followed through by the British Beer & Pub Association (BBPA),¹²² which published its revised Framework Code of conduct in 2005, with members including the major pubcos reviewing their codes in line with it.¹²³

¹¹⁶ Ibid at para 199, p56

¹¹⁷ The British Beer & Pub Association (BBPA) code of practice had not been updated since 1997, with the TIC recommending this be done as a matter of urgency. (Ibid at para 203, p57)

¹¹⁸ Ibid at para 204, p57

¹¹⁹ Trade and Industry Committee, *Pub Companies: Response to the Committee’s Second Report of Session 2004-05* (HC 2004-05, 434)

¹²⁰ Ibid at para 2, p1

¹²¹ Ibid at p2-3

¹²² The BBPA is the leading body representing pubcos and brewers in Britain.

¹²³ Business and Enterprise Committee, *Pub Companies* (HC 2008-2009, 26-1) at para 23, p12

3.2 OFT – continued decline to investigate the market

Notwithstanding the publication of the revised Framework Code, given its voluntary nature and the Government's apparent lack of interest in intervening in the market, it was of little surprise that the competition concerns over the supply of beer in the UK market did not dissipate. In March 2005, the Competition Commission considered the merger of Serviced Dispense Equipment Limited (SDEL) and Coors' technical services function.¹²⁴ Having concluded that the merger would result in a substantial lessening of competition in the technical services market, the Competition Commission believed that as the price for the supply of technical services and equipment were almost always bundled with the price of a barrel of beer, it recommended the OFT once again consider whether a market investigation into the pricing or supply of beer was appropriate.¹²⁵ In keeping with its on-going resistance to further investigate the market, the OFT later in 2005 declined to conduct a new inquiry into the distribution of beer to public houses.

3.3 BISC's heightened concerns

Despite the OFT's increasingly unfaltering support for the beer tie which was in line with the EU's acceptance of it as a legitimate business model, the relative inaction in dealing with the foregoing concerns raised in regard to the UK market caused the investigation and reporting on it to continue in earnest.

The Business and Enterprise Committee, now the Business Innovation and Skills Committee (BISC), re-visited this in 2009. They reviewed the relationship between pubcos and their tenants in light of the TIC's 2004 findings, resulting in a scathing report.¹²⁶ Contrasting with the 2004 conclusion already mentioned that the 'quantifiable costs of the tie were usually balanced by the benefits available to the tenants', it clearly stated it had "no confidence that the advantages of the tie outweigh its drawbacks."¹²⁷ They considered the best way to test this was by requiring that on renewal of their lease, lessees be offered the choice of being tied or free of tie.¹²⁸ The BISC stated that a voluntary arrangement implementing this would be preferable to a statutory solution however they considered it unlikely that pubcos would support it. It was therefore suggested that the department of

¹²⁴ Competition Commission, *Serviced Dispense Equipment Limited and the Technical Services Function of Coors Brewers Limited. A report on the proposed acquisition by Serviced Dispense Equipment Limited of the Technical Services Function of Coors Brewers Limited* (March 2005). Technical services equipment is used to dispense draught beer and cider at outlets with technical services including the installation, servicing and removal of such equipment (at para 3, p3)

¹²⁵ Ibid at para 37, p8

¹²⁶ Business and Enterprise Committee, *Pub Companies* (HC 2008-2009, 26-1)

¹²⁷ Ibid at p4

¹²⁸ Ibid at p4

Business Innovation and Skills consider how best to bring this about and to conduct an urgent consultation on the phasing of this proposal.¹²⁹ While it was considered to be highly likely that the tie pushed up beer prices for lessees and customers, given the unforeseen consequences of the Beer Orders discussed in Chapter 2, they expressed a reticence in suggesting ‘eye-catching recommendations’, such as the abolition of the tie.¹³⁰ These had the potential to produce problems worse than those they sought to solve.¹³¹ It was also noted that the TIC’s main recommendation, namely the introduction of a new updated framework code of conduct, had been implemented with all pubcos who responded to the BISC claiming to have complied with this, although some of its recommendations had been completely rejected.¹³² Nevertheless given the level of acrimony in the market, which was evident in the terms of the foregoing reports, the BISC found that lessees were far less positive than pubcos regarding progress made since 2004 noting that “*much of their evidence is completely at odds.*”¹³³

3.3.1 Competition issues pre-Beer Orders still evident in the UK market

In contrast to the OFT’s 2000 report,¹³⁴ the BISC reported that many of the concerns raised in the MMC’s 1989 Report discussed above “*can be found in the market today.*”¹³⁵ They referred to evidence from the Campaign for Real Ale (CAMRA) that the on-trade price of a pint of beer in 2008 could be estimated to be approximately 3.3 to 3.5 times more than the off-trade price.¹³⁶ Whilst it was acknowledged that the evidence relating to the tie’s impact on pricing was not altogether simple, given the large market share enjoyed by pubcos, it was suggested their prices set the norm which was followed by the market, with the exception of some occasional discounts.¹³⁷ The BISC also found the MMC’s concerns regarding consumer choice remained as pubcos restrict the list of approved products, impacting on lessees’ ability to respond to the market and to stock smaller brewers products.¹³⁸ Tenants’ bargaining position was also considered not to have improved since 1989 given their limited bargaining position compared to pubcos.¹³⁹ They were therefore unable to negotiate discounts, guest ale provisions or lower rents which would ultimately

¹²⁹ Ibid at para 139, p53

¹³⁰ Ibid at p4 and para 11, p8

¹³¹ Ibid at para 11, p8

¹³² Such as the requirement that pubcos advise their tenants on the average discount received from breweries as this was deemed commercially sensitive. (Ibid at para 24-26, p12-13)

¹³³ Ibid at para 27, p13

¹³⁴ Above, n.103 and Chapter 2

¹³⁵ Above, n.126 at para 160, p61

¹³⁶ Ibid at para 161-162, p62

¹³⁷ Ibid at para 163, p63

¹³⁸ Ibid at para 164, p63

¹³⁹ Ibid at para 165, p63-64

benefit consumers through lower prices and increased choice.¹⁴⁰ Further, one of the principle concerns expressed by the MMC in 1989 was the lack of an independent wholesale and distribution sector in the UK market. The BISC subsequently received evidence in support of CAMRA's claim that the pub market is 'substantially foreclosed' to small brewers due to their difficulties in meeting pubco demands and the logistical issues in supplying their tied estates, with only three pubcos supporting SIBA's DDS discussed above.¹⁴¹

3.3.2 The OFT's position

While this report was produced five years after the TIC reported in 2004 with significant competitive issues still being apparent in the UK beer market, when invited to comment on the foregoing the OFT declined to alter its position as submitted to the TIC in 2004 that "*there is no significant competition problem in relation to the beer and pub market.*"¹⁴² The BISC noted its disagreement with this in light of the evidence it had received in the course of this enquiry which demonstrated that there was a case for the OFT to investigate.¹⁴³ It noted that since 2004 brewery discounts had increased significantly however very little of these have been passed on through the supply chain to the benefit of lessees or customers.¹⁴⁴ While the OFT in 2004 submitted that pubcos were driving down wholesale prices,¹⁴⁵ the BISC had established that pubcos did little to resist increases in list prices, on which the customer retail price is based.¹⁴⁶ This was due to the fact that pubco discounts increased pro rata with brewery list price increases.¹⁴⁷ The resulting divergence in on and off-trade beer prices had caused pub closures and increased supermarket beer sales.¹⁴⁸ The BISC was also critical of the OFT's refusal to recognise the public house market as a separate market from other on-trade premises.¹⁴⁹ The BISC considered pubs to form a distinct segment of the on-licensed market. While there may be difficulties in distinguishing food-led pubs and restaurants, they generally considered there was a distinction between pubs and other on-trade outlets with this being well recognised by the

¹⁴⁰ Ibid at para 165, p63-64

¹⁴¹ Ibid at para 166-167, p64

¹⁴² Ibid at para 169, p65. Trade and Industry Committee, *Pub Companies Volume II* (HC 2004-2005, 128-II) at Appendix 22, Ev 232

¹⁴³ Above, n.126 at para 169, p65

¹⁴⁴ Ibid at para 170, p65-66 and Trade and Industry Committee, *Pub Companies Volume II* (HC 2004-2005, 128-II) at Appendix 22, para 9, Ev 233

¹⁴⁵ Trade and Industry Committee, *Pub Companies Volume II* (HC 2004-2005, 128-II) at Appendix 22, Ev 233

¹⁴⁶ Above, n.126 at para 171, p66

¹⁴⁷ Ibid at para 171, p66

¹⁴⁸ Ibid at para 171, p66

¹⁴⁹ Ibid at para 172, p66

consumer.¹⁵⁰ Reference was also made to the OFT's omission in 2004 to have regard to the geographical market.¹⁵¹ They suggested that in relation to public houses this was likely to be narrowly defined, with the market for substitutable pubs being within a radius of 10-15 miles, as this was the maximum distance within which a consumer was likely to travel to visit a pub for a drink.¹⁵² The OFT however only considered data on a local licensing authority basis.¹⁵³ In light of the foregoing the BISC was rightly 'surprised and disappointed' by the OFT's reluctance to investigate whether the pub market was working well for consumers.¹⁵⁴ This was especially given the pubcos' failure to pass on discounts to lessees which in turn prevented consumers from benefitting from lower prices. This was deemed to have contributed to the disparity between on and off-trade prices and so contributed to the on-going closure of pubs in the UK as consumers turned to cheaper off-trade sales.¹⁵⁵ It was subsequently deemed to be *"to the overall detriment of the consumer if pubs are forced to close due to uncompetitive practices in the market."*¹⁵⁶

3.3.3 Underestimation of the costs of the tie

The BISC reiterated that the beer tie generally benefits from the EU Block Exemption Regulation on the basis that it offers low cost entry to the business for lessees accepting the tie, and in the UK is excluded from the Chapter I prohibition of the 1998 Act.¹⁵⁷ Nevertheless, the BISC considered that the benefit of low cost entry offered by the pubco lease model should not be overstated with there being no evidence of tied lessees enjoying benefits that are not available to free-of-tie tenants or freeholders.¹⁵⁸ The high failure rate of tied public houses was considered to be attributable to the speed with which wholesale prices offered to tied lessees have increased thereby placing them at a significant competitive disadvantage compared to free-of-tie tenants.¹⁵⁹ The BISC therefore considered that the beer tie operated by pubcos may be anti-competitive and in light of the OFT's unwillingness to seriously investigate the matter, the Secretary of State, rather than the OFT, was urged to refer the beer tie to the Competition Commission to conduct a

¹⁵⁰ The BISC pointed to the presentation of a pub internally and externally, the range of services provided and prices as factors contributing to the distinction. Above, n.126 at para 172, p66-67

¹⁵¹ Ibid at para 173, p67

¹⁵² Ibid at para 173, p67

¹⁵³ Ibid at para 173, p67

¹⁵⁴ Ibid at para 174, p67

¹⁵⁵ Ibid at para 174, p67

¹⁵⁶ Ibid at para 174, p67. The BISC also considered the practice of pubcos imposing restrictive covenants on the sale of pubs however this is not considered here.

¹⁵⁷ Ibid at para 179-180, p68-69

¹⁵⁸ Ibid at para 183, p69

¹⁵⁹ Ibid at para 184, p69-70

market investigation.¹⁶⁰ The BISC's provisional view was that steps be taken to significantly restrict the tie in order to restore competition to the retail market, although similarly cautious to the TIC, it reiterated that severing the tie could simply result in one set of powerful players being replaced with another, as well as having a detrimental effect on small brewers.¹⁶¹ Consequently, it was becoming increasingly clear that the consequences of the Beer Orders had potentially had a chilling effect with regard to suggesting any further significant interventions in the UK beer market.

3.4 CAMRA Super-Complaint

Despite the strong terms of the 2009 report, the Government's response was not as prompt as expected, with this being attributed to the significant developments following its publication, namely CAMRA's intention to launch a super-complaint.¹⁶² This was submitted to the OFT in 2009 on the basis that the UK pub industry, and the beer tie in particular, were anti-competitive.¹⁶³ The complaint primarily concerned exclusive purchasing obligations under the beer tie focusing on pubcos which tie over five hundred pubs in the UK in relation to beer.¹⁶⁴

CAMRA claimed there was a number of serious market failures stemming from the fact that there are 57,000 public houses in the UK of which 54% are leased or tenanted by a brewing or non-brewing pub owning company and in almost all cases were subject to a beer tie.¹⁶⁵ They considered that the cumulative effect of this was to foreclose a substantial part of the UK market to brewers; to foreclose access to suppliers of technical services and equipment to a substantial part of the UK pub market; to hinder access of suppliers of other goods and services subject to exclusive purchasing obligations, to the UK pub market; and to hinder the access of wholesalers to the UK pub market.¹⁶⁶ Access to these tied outlets via the tying company was not considered to be a substitute for independent access, which allowed companies to negotiate on an individual basis with each tied pub.¹⁶⁷ The operation of the beer tie and associated exclusive purchasing obligations was therefore deemed to

¹⁶⁰ Ibid at para 190, p71

¹⁶¹ Ibid at para 191, 71

¹⁶² Business and Enterprise Committee, *Pub Companies* (HC 2008-2009,798) at para 1, p1

¹⁶³ Campaign for Real Ale, *UK Pub Market Super Complaint, A Fair Share for the Consumer_Memorandum to the Office of Fair Trading (Campaign for Real Ale, 2009)*. The focus here is the arguments regarding the competitive aspects of the tie, not the general relationship between the pubco and tenants/ lessees including matters such as rent calculations and dispute resolution.

¹⁶⁴ Ibid at para 4.3, p7-8

¹⁶⁵ CAMRA's concerns were focused on those companies tying 500 or more public houses. When companies tying fewer pubs were excluded this fell to 41%. Ibid at para 1.2, p3

¹⁶⁶ Ibid at para 1.3, p3-4. Technical services is not considered here

¹⁶⁷ Ibid at para 1.3, p3-4

prevent, restrict and distort competition by establishing a substantial barrier to market entry and so infringed Article 101(1) TFEU.¹⁶⁸

In light of the foregoing, CAMRA submitted that whilst the benefits of the operation of the beer tie were clear from the perspective of the tying company, consumers did not receive a “*fair share of the resulting benefit*”.¹⁶⁹ They therefore claimed that pubcos should be precluded from relying on Article 101(3) TFEU to exempt their agreements from Article 101(1) TFEU.

In turning to the issue of market definition, similarly to the BISC, CAMRA urged the OFT to regard the public house market as a separate market from other on-trade premises and made reference to numerous factors in support of this.¹⁷⁰ With regard to geographical scope, they asserted that competition occurred at a local level with consumers only being prepared to travel short distances when deciding where to drink.¹⁷¹ Consequently while it was recognised that no company controlled more than 15% of the UK’s pubs, the ‘local nature’ of the pub market meant that the situation still resulted in substantial consumer detriment.¹⁷² Further, various market failures including the barriers to market entry faced by small brewers; and the role of the beer tie in enabling pubcos to increase retail prices above market levels and so prompting pub closures all contributed to this consumer detriment.¹⁷³ CAMRA submitted that pubcos were protected from competition in the supply of ‘tied’ products to their estates as competitors are denied access to these captive outlets. This resulted in higher prices for consumers as tied pubs are precluded from sourcing their supplies on the free market.¹⁷⁴ There was deemed to be a lack of price competition in the UK pub market as a whole as these tied pubs were prohibited from competing with free and managed pubs on the basis of price, which also meant free and managed pubs were able to charge higher prices than would be possible if there was real competition.¹⁷⁵ CMARA also pointed to the difficulty experienced by small brewers in

¹⁶⁸ Above, n.163 at para 1.3, p3-4

¹⁶⁹ Ibid at para 1.4, p4

¹⁷⁰ Ibid at para 6.2, p11

¹⁷¹ Ibid at para 7.1, p13. CAMRA stated that when competition concerns are assessed through analysis of local authority areas, the use of isochrones is necessary in order to accurately assess local competition between pubs (ibid at para 7.2-7.3, p13). This means within a set radius which is measured by walking time or distance around a particular pub. See Office of Fair Trading, *CAMRA Super-complaint – OFT Final Decision* (OFT 1279, 2010) at para 5.18, p72

¹⁷² Above, n.163 at para 1.5, p4

¹⁷³ Ibid at para 1.5, p4

¹⁷⁴ Ibid at para 3.2, p6

¹⁷⁵ Ibid at para 3.3, p6

accessing the market as causing there to be a lack of consumer choice, with restrictive covenants on the sale of properties causing further loss of amenity.¹⁷⁶

In light of the foregoing, CAMRA's optimum super complaint outcome was for the OFT to conduct a market study into the beer tie; public house rental calculations; and the use of restrictive covenants to restrict the availability of free-of-tie pubs.¹⁷⁷ They therefore focused on the need for the tie to be reformed in order to prevent its exploitation.

3.4.1 The OFT's Initial Response to the super-complaint

The OFT issued its initial response to CAMRA's super complaint in October 2009.¹⁷⁸ Despite the arguments presented by CAMRA and the BISC's 2009 conclusion noted above that it had "*no confidence that the advantages of the tie outweigh its drawbacks*," in keeping with its past reluctance to reconsider the beer tie, the OFT concluded that it "*has not found evidence of competition problems that are having a significant impact on consumers*."¹⁷⁹ As they had done previously they referred to the large number of competing pub outlets owned by different operators at the national, regional and local level with consumers benefitting from competition and choice between different pubs.¹⁸⁰ The commercial interests of pubcos were aligned with their lessees, as any competitive strategy that compromised the competitive position of lessees would cause them both sales and margin losses.¹⁸¹ They also failed to consider that tied lease agreements prevented pubcos from offering consumers a wide choice as pubcos generally sourced from a number of suppliers.¹⁸² The OFT therefore concluded that overall no further investigation of the competition problems in the UK beer and pub market was warranted.¹⁸³ As they had done before, they refused to undertake a market study or investigation under the 1998 Act or to make a reference to the Competition Commission.¹⁸⁴ They therefore rejected the complaint in October 2009 prompting CAMRA to appeal to the Competition Appeals Tribunal

¹⁷⁶ Ibid at para 3.4-3.5, p6

¹⁷⁷ Ibid at para 18.1, p28

¹⁷⁸ Office of Fair Trading, *Response to CAMRA'S super-complaint* (OFT 1137, 2009)

¹⁷⁹ Ibid at p6

¹⁸⁰ Ibid at p6

¹⁸¹ Ibid at p6

¹⁸² Ibid at p6

¹⁸³ Ibid at p7

¹⁸⁴ Ibid at p8

(CAT),¹⁸⁵ whilst the OFT undertook a public consultation with a view to further considering the alleged anticompetitive behaviour of pubcos.¹⁸⁶

3.5 The BISC's Follow-Up

In the meantime, the BISC again contrasted with the OFT's position on the market by restating in 2010 its commitment to the recommendations in its 2009 report on pubcos.¹⁸⁷ It also added that a reference to the Competition Commission may be necessary as it had “grave doubts about the industry's willingness to do enough voluntarily to prevent statutory or regulatory intervention.”¹⁸⁸ Given that since the decision to revoke the Beer Orders in 2000, notwithstanding the numerous investigations into the market, the only meaningful action taken to address these on-going concerns was the introduction of the BBPA's revised voluntary Code of Practice, the BISC unsurprisingly found the industry had only made ‘modest’ progress in the year since its last report. It therefore suggested that the Code had to be treated by major pubcos as an ‘absolute *de-minimis* requirement’, with its successful ‘policing’ being critical to the success of the reforms.¹⁸⁹ Again whilst they acknowledged that many advocated the removal of the beer tie, it remained committed to its 2009 view that the only way to properly judge the fairness of the tie was to offer lessees the possibility of being tied or free of tie.¹⁹⁰ June 2011 was set as the deadline for real reform, thereby giving the industry a further two years to address these on-going issues even although it had already shown itself incapable, after which it would recommend legislation as a basis for statutory regulation.¹⁹¹ In acknowledgement of the numerous occasions on which the industry had been ‘found wanting’, this was the last opportunity for pubcos to instigate effective self-regulation to remove anticompetitive concerns.¹⁹² The BISC did however strongly encourage the Government to monitor the success of the initiative for reform and to remain open to a reference to the Competition

¹⁸⁵ CAMRA applied to have its application to the CAT withdrawn following the OFT's final decision on its super complaint, namely that it would not take any further action on the beer tie or the pubco model. (See Office of Fair Trading, *CAMRA super-complaint – OFT final decision* (OFT 1279, 2010).) Permission to have its application to the CAT withdrawn was granted on 7th February 2011. See Campaign for Real Ale v. Office of Fair Trading (1148/6/1/09) Order of the Tribunal, (Competition Appeal Tribunal, 7 February 2011) <http://catribunal.org/files/1148_CAMRA_order_070211.pdf> accessed 2nd July 2015

¹⁸⁶ Office of Fair Trading, *CAMRA super-complaint – OFT final decision* (OFT 1279, 2010). This is discussed below.

¹⁸⁷ Business Innovation and Skills Committee, *Pub Companies: Follow-Up* (HC 2009-2010, 138) This was more concerned with the relationship between tied lessees and their landlord pubco than with the competitive aspects of the tie.

¹⁸⁸ Ibid at p3

¹⁸⁹ Ibid at p3

¹⁹⁰ Ibid at p4

¹⁹¹ Ibid at para 32, p54

¹⁹² Ibid at p4

Commission, while also encouraging the OFT to reconsider and carefully review the issues raised by CAMRA in their super-complaint.¹⁹³

3.5.1 Government's apparent support for reform

In a departure from its long held stance that intervention in the market was not required, the Government's response to the foregoing report was that as part of its broader strategy on pubs, it "*wholeheartedly endorsed*" the recommendations made.¹⁹⁴ The BISC considered this to amount to "*effective adoption*" of all of its recommendations, including the June 2011 deadline.¹⁹⁵ The Government clarified that it accepted the proposals for the effective operation of the BBPA code of conduct and also stated that it should incorporate the option for tenants to be tied or free of tie, and the industry should offer a voluntary guest beer outside the tie as part of the code.¹⁹⁶

3.6 Super Complaint - the OFT's final decision

While this was a remarkably positive response from the Government, it was followed shortly after in October 2010 by the OFT's final decision on CAMRA's Super-Complaint.¹⁹⁷ The OFT stated that in reaching its decision it had reviewed all of the responses received to its consultation mentioned above.¹⁹⁸ In-keeping with its long held position that it has already reviewed the beer tie, as have the Competition Commission¹⁹⁹ and the European Commission, the OFT predictably re-iterated its initial finding that no further evidence had been presented to justify initiating any additional investigations.

3.6.1 The OFT's assessment

The OFT responded to each aspect of the super-complaint, dismissing each in turn.²⁰⁰

¹⁹³ Ibid at para 160, p48

¹⁹⁴ Business innovation and Skills Committee, *Pub Companies: follow Up: government response to the committee's 5th report of session 2009-10* (HC 2009-2010, 503) at para 3, p3. This commitment was made by the then Labour Government however the new coalition also supported this approach.

¹⁹⁵ Ibid at para 3-4, p3

¹⁹⁶ Ibid at para 6, Appendix 1, p6

¹⁹⁷ Above, n.186

¹⁹⁸ Ibid at p6

¹⁹⁹ Formerly the MMC. At the time of the report the new Coalition Government was in power

²⁰⁰ Not every aspect can be covered here. Only the main points regarding the competitive implications of the tie will be discussed.

3.6.1.1 Competitive market, alignment of the interests of pubcos and tenants and rising retail prices explained

At the outset the OFT stated that its focus was whether there was effective competition benefitting consumers within the beer and pub market.²⁰¹ For the purpose of its competitive assessment the OFT considered the level of competition between pubs.²⁰² They did not however take as narrow an approach to the relevant geographical market as that suggested by CAMRA. Consideration was had to the level of competition between pubs owned by different operators on the basis of both Local Authority licensing areas and an analysis of the number of competing premises within clear distances around pubs in the UK.²⁰³ The OFT noted that “[a]t a national, regional and local level, the evidence indicates that there is a large number of competing pub outlets owned by different operators and that there is competition and choice between different pubs.”²⁰⁴ No individual pubco was found to hold a significant concentration of public houses.²⁰⁵ The resulting fragmented nature of the market was deemed not to facilitate co-ordinated behaviour, and so pubcos could not sustainably inflate prices above a competitive level as had been suggested by CAMRA.²⁰⁶ They also established that it would not be sustainable for pubcos to set prices and rents at a level that would risk the competitive position of the pubs within their estate as this would result in a loss of custom to other pubs in their locality.²⁰⁷ Consequently they concluded that the commercial interests of pubcos and their lessees were aligned.

The OFT was satisfied that increased retail prices were attributable to increased costs at the retail level of the supply chain due to inflation rates and were not due to a lack of effective competition between pubs, as had been submitted by CAMRA.²⁰⁸ While it was accepted that on average tied pubs charged more for beer than free and managed houses, this could be explained by the ‘package of features’ offered by a pub to customers, and it was also considered that average prices disguised the variations in prices charged by different pubs.²⁰⁹ Additionally, in addressing tenants’ concerns over the prices and rent levels paid to their landlords, noting the large number of submissions received to that effect, the OFT

²⁰¹ Above, n.186 at p6

²⁰² In previous merger decisions ‘pub’ included other licensed premises such as bars and inns but not clubs or restaurants. (Above, n.186 at para 5.13, p70.) The OFT did not however deem it necessary to reach a conclusion regarding market definition and so did not preclude that pubs may compete in a wider retail market with other on-trade premises (ibid at para 5.14, p70).

²⁰³ Above, n.186 at para 5.21, p73

²⁰⁴ Ibid at p6-7

²⁰⁵ Ibid at p11

²⁰⁶ Ibid at para 5.160-5.161, p125

²⁰⁷ Ibid at para 5.162, p125

²⁰⁸ Ibid at para 5.166, p126

²⁰⁹ Ibid at para 5.166, p126

relied on its own conclusion that there was significant competition and choice between pubs so it was unlikely that issues relating to the negotiation process would result in consumer detriment.²¹⁰ Consequently this was not an issue relating to competition and was ultimately for pubcos and their lessees to address.²¹¹

3.6.1.2 Barriers to entry to brewers and wholesalers

The OFT also turned to the considerable and well documented concerns over market foreclosure and the resulting exclusion of small brewers and wholesalers from the market. They did not consider that large pubcos' reliance on beer tie agreements prevented pubs from offering consumers a wide choice of beers due to their practice of multi-sourcing from a range of suppliers.²¹² Despite the concerns expressed by the TIC, BISC and CAMRA noted above regarding small brewers' access to pubcos tied estates, the OFT stated that "[t]here appear to be considerable opportunities for access to pubs and other on-trade outlets by brewers".²¹³ Whilst this statement was most accurate for larger brewers, it was arguably not so for smaller producers. However, the OFT stated that the logistical issues faced by these small brewers in dealing with retail chains with large-scale distribution networks did not in themselves indicate a problem of competition.²¹⁴ This was notwithstanding the considerable lack of independent wholesalers in the UK market as well as the domination of the distribution sector by the largest international brewers which had been a source of concern in previous enquiries.²¹⁵ The OFT stated that whilst small brewers may have difficulty accessing the pubcos centralised distribution systems, these resulted in efficiencies and enabled some brewers to achieve large-scale distribution which in turn facilitated market entry or expansion.²¹⁶ These benefits had clearly been enjoyed by the largest international brewers who supplied the pubcos estates. Further, SIBA's DDS was highlighted as a 'successful market led solution to the issues faced by small brewers' notwithstanding pubcos very limited participation in this scheme mentioned above.²¹⁷

²¹⁰ Ibid at p7

²¹¹ Ibid at p7

²¹² Ibid at p7

²¹³ Ibid at para 4.64, p64

²¹⁴ Ibid at para 4.67, p65

²¹⁵ See for example TIC's 2004 Report discussed above

²¹⁶ Above, n.186 at para 4.66-4.67, p65

²¹⁷ Ibid at para 4.68, p65

3.6.1.3 No further investigation

In light of its foregoing conclusions, the OFT stated that it did not have to address the availability of an appropriate remedy in response to CAMRA's complaint.²¹⁸ It also noted that under Article 3(2) of Regulation 1/2003,²¹⁹ it is not possible for national law to prohibit agreements which may affect trade between Member States but do restrict competition within the meaning of Article 101(1) TFEU, fulfil the conditions of Article 101(3) TFEU or benefit from a block exemption Regulation.²²⁰ The OFT again deferred to the fact that the European Commission and Courts have found that Article 101(1) TFEU does not apply to tied leases where the pubco sources from a number of sources, or the agreements are *de minimis*.²²¹ Dismissing the extensive concerns raised by CAMRA, the OFT did not consider that further investigation of the beer and pub market was warranted concluding that it "*has not found evidence of competition problems that are having a significant impact on consumers.*"²²² No specific recommendations were therefore made to the Government or the industry as a result of its consideration of the issues raised by CAMRA.²²³

3.7 BISC's Persistence

While the OFT continued to decline to interfere in or recommend further investigation of the market, with the support of the new coalition Government, the BISC honoured its undertaking to monitor progress. In September 2011 it published its fourth report on pubcos in seven years, and assessed whether the industry had delivered on its promise of 'meaningful reform'.²²⁴ The significantly contradictory evidence received by the BISC was deemed an indication of how little the industry had moved on.²²⁵ Whilst there had been some improvements, a genuine commitment to reform was clearly lacking and so the test set by its predecessor Committee had not been met.

3.7.1 Lack of meaningful reform and demands for a statutory code

As noted above, the BISC had previously advocated that the on-going dispute regarding the beer tie could be ended by offering lessees the option of being tied or free of tie,

²¹⁸ Above, n.186 at para 9.40, p155

²¹⁹ Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty (2003) OJ L1/1

²²⁰ Above, n.186 at para 9.41, p155

²²¹ Ibid at footnote 277, p155

²²² Ibid at p6

²²³ Ibid at para 9.46, p157

²²⁴ Business Innovation and Skills Committee, *Pub Companies* (HC 2010-12, 1369-I) at para 154, p50

²²⁵ Ibid at para 8, p7

thereby enabling both sides to prove their respective claims. The Government also ‘wholeheartedly’ endorsed this proposal. The BBPA submitted that whilst there was no explicit free-of-tie option under the existing voluntary Framework Code, companies were not precluded from offering this.²²⁶ Numerous pubcos provided evidence of offering free-of-tie arrangements to lessees, however, evidence was also provided that only 16% of new lessees and 9% of existing lessees had been offered a free-of-tie option.²²⁷

This inaction was deemed by the BISC to highlight the industry’s inability, or more likely, unwillingness, to deliver meaningful reform.²²⁸ Its inability to do so despite clear instruction demonstrated “*the deep-seated problems which lie at the heart of the industry*”.²²⁹ Although the new Codes of Practice implemented since its last report were deemed to be an improvement, they only addressed a limited number of issues.²³⁰ As noted above, the BISC’s 2010 report had been lauded as the final opportunity for the industry to reform and it had failed to do so.²³¹ The BISC deemed there to be no alternative but for the Government to put the industry’s Code on a statutory footing and for it to be accompanied by a statutory Code Adjudicator.²³²

4. Government’s inaction

Despite the apparent zest for change expressed in its response to the BISC’s 2010 report discussed above, the Government reneged on this when statutory intervention was deemed immediately necessary. Consequently the Government could be seen to be reverting to its long held reticence to engage in actual reform of the market. This inaction subsequently prompted a further flurry of investigations and reporting on the market, the terms of which initially broadly echoed those discussed above although they would soon recognise the need for genuine reform.²³³

²²⁶ Ibid at para 149, p48

²²⁷ Ibid at para 149, p48 and para 152, p49

²²⁸ Ibid at para 153, p49

²²⁹ Ibid at para 154, p50

²³⁰ Ibid at para 154, p50

²³¹ Ibid at para 156, p50

²³² Ibid at para 157, p50

²³³ Concern over pubco practices prompted the introduction of the Tied Public Houses (Code of Practice) Bill to Parliament in March 2011 under the Ten Minute Rule, ‘MP Martin Horwood seeks end to ‘unfair’ tied pubs’ (*BBC*, 9th March 2011) <<http://www.bbc.co.uk/news/uk-england-gloucestershire-12695163>> accessed 3rd July 2015. Echoing the BISC’s recommendations this proposed the introduction of a statutory code of practice under which pubcos had to offer tenants a guest beer option as well as a free-of-tie option. The Bill failed to complete its passage through Parliament.

4.1 Self-regulation over statutory regulation

In determining ‘the most appropriate course of action’ in response to the BISC’s 2011 report, the Government defaulted to the OFT’s position that there was no evidence of competition problems having an adverse impact on consumers.²³⁴ Further out of line with its response to the BISC’s 2010 report, the Government stated that “*legally binding self-regulation can be introduced far more quickly than a statutory solution and can, if devised correctly, be equally effective*”.²³⁵ Whilst this statement was generally correct, it was inaccurate in the circumstances of this market, as it had clearly failed to change significantly following years of voluntary regulatory attempts.

The Government nevertheless placed reliance on the EU’s acceptance of the beer tie under the EU Block Exemption Regulation, which had been recently renewed.²³⁶ Apparently disregarding the preceding dearth of reports published on the matter it stated that it should “*not intervene in setting the terms of commercial, contractual relationships, where these are fully justified by law and have been found by the OFT to be raising no competition issues that significantly affect consumers*”.²³⁷ In finding a solution to the issues presented, it contrasted starkly with its response to the BISC’s 2010 report, stating that it “*considers the debate over ‘tied’ or ‘free-of-tie’ to be largely a distraction. There is nothing in itself that causes the tie to be fundamentally wrong*”.²³⁸ The new coalition Government therefore appeared to shun the BISC’s proposal for statutory regulation as endorsed by its predecessors. Despite acknowledging the industry’s history of failed attempts at self-regulation, it was proposed that a legally binding self-regulatory code be adopted, with it naively stating that “*the industry will lose no time in fulfilling the commitments it has publicly made*”.²³⁹ This policy change notwithstanding the past gross inaction of the industry prompted suggestions that, in addition to OFT and EU policy, the BBPA had been significantly influential.

²³⁴ Business Innovation and Skills Committee, *Government response to the HOC BISC 10th Report of Session 2010-2012: Pub Companies* (Cm 8222, 2011) at p3

²³⁵ Ibid at p3

²³⁶ Ibid at p7

²³⁷ Ibid at para 16, p7

²³⁸ Ibid at para 28, p9

²³⁹ Ibid at para 70, p16

4.2 Self-regulation: the response

Suspensions over the BBPA's involvement were raised in December 2011, when the BISC followed up on the Government's response to its 2010 report.²⁴⁰ This detailed the mechanics implementing the legally binding code which would no longer be on a statutory basis.²⁴¹ The All-Party Parliamentary Save the Pub Group²⁴² stated it was "*extremely unhappy*" with the Government's response to the BISC's report which reneged on its undertaking to introduce a statutory code as well as a free-of-tie option and a guest beer right for tied tenants.²⁴³ Their concerns included the fact that the code was the product of closed negotiations with the BBPA.²⁴⁴ A genuine free-of-tie option and guest beer provision were deemed necessary to reduce the over-inflated price of tied products with their omission rendering the proposed reforms "*weak and ineffectual*."²⁴⁵ Concerns were also raised over the failure to establish mechanisms to review the BBPA's commitment to deliver reform in light of its past failings.²⁴⁶ These concerns were echoed amongst numerous interested parties, including the Association of Licensed Multiple Retailers (ALMR).²⁴⁷ Consequently, the general consensus rightly appeared to be that these reforms were entirely unsuitable to address the on-going problems of the beer tie and the industry generally.

²⁴⁰ Business Innovation and Skills Committee, *Pub companies: Follow up to the Government Response* (20th December 2011, Version II)

²⁴¹ The code would be on a contractual basis between the pubco and their lessee or tenant, with non-compliance amounting to a breach of contract. (Ibid at 'Written Evidence submitted by the Department for Business, Innovation and Skills'). Pubcos undertook to incorporate this into new leases and committed to enter new agreements with existing tenants and lessees by the end of 2011. (Ibid at 'Written Evidence submitted by the Department for Business, Innovation and Skills') Regarding the interaction between the new code and Scottish law, it was established that the legal principles applicable in both jurisdictions were very similar. (Ibid at 'Supplementary written evidence submitted by Department for Business, Innovation and Skills'). The Scottish position is not discussed further.

²⁴² This Group brings together the members of the House of Commons and the House of Lords who want to assist in preserving and protecting the British pub.

²⁴³ Above, n.240 at 'Further written evidence submitted by Fair Pint Campaign'

²⁴⁴ Ibid at 'Written Evidence submitted by the All-Party Parliamentary Save the Pub Group'

²⁴⁵ Ibid at 'Written Evidence submitted by the Department for Business, Innovation and Skills' and 'Written evidence submitted by the All-Party Parliamentary Save the Pub Group'

²⁴⁶ Ibid at 'Written Evidence submitted by the All-Party Party Parliamentary Save the Pub Group'

²⁴⁷ The ALMR is a network of retailers which champion smaller independent companies which own and operate public houses. Association of Licensed Multiple Retailers, 'About us' (*Association of Licensed Multiple Retailers*) <<http://www.almr.org.uk/about/>> accessed 3rd July 2015

4.3 Demands for an independent inquiry into reform

A backbencher business debate in January 2012 forced the Government to re-visit the issue of the beer tie as pub closures continued to increase around the UK.²⁴⁸ MPs called for an industry wide statutory code of conduct including a genuine free-of-tie option and an open market rent review, overseen by an independent body.²⁴⁹ The outcome was unanimous support for the Government to instruct an independent review of self-regulation within the pub industry, reporting in Autumn 2012.²⁵⁰

5. Government's policy change

The aforementioned report failed to materialise and in January 2013 the Business Secretary undertook to consult on the establishment of a statutory Code and an Adjudicator to oversee the relationship between pubcos and licensees, as recommended by the BISC in 2010.²⁵¹ However at the outset of its consultation document the Government sought to clarify that this was not a competition issue, again deferring to the OFT's 2010 finding noted above that *"[a]t a national, regional and local level, the evidence indicates that there is a large number of competing pub outlets owned by different operators and that there is competition and choice between different pubs."*²⁵² It was however stated that whilst the tie is a good business model when it is operated responsibly, its abuse could

²⁴⁸ HC Deb 12th January 2012, col 351

<<http://www.publications.parliament.uk/pa/cm201212/cmhansrd/cm120112/debtext/120112-0002.htm-12011294000002>> accessed 7th May 2015. BBC News, 'MPs call for urgent action to tackle pub closures', (BBC, 12 Jan 2012)

<<http://news.bbc.co.uk/1/hi/health/10675000/10675903.stm>> accessed 3rd July 2015) and J Charlton and P Wintour, 'Pub Companies' regulation to be subject of independent inquiry' (The Guardian, 12th January 2012) <<http://www.guardian.co.uk/business/2012/jan/12/pub-companies-regulation-independent-inquiry>> accessed 3rd July 2015

²⁴⁹ HC Deb 12th January 2012, col 400

<<http://www.publications.parliament.uk/pa/cm201212/cmhansrd/cm120112/debtext/120112-0002.htm-12011294000002>> accessed 7th May 2015. J Charlton and P Wintour, 'Pub Companies' regulation to be subject of independent inquiry' (The Guardian, 12th January 2012) <<http://www.guardian.co.uk/business/2012/jan/12/pub-companies-regulation-independent-inquiry>> accessed 3rd July 2015)

²⁵⁰ HC Deb 12th January 2012, col 400

<<http://www.publications.parliament.uk/pa/cm201212/cmhansrd/cm120112/debtext/120112-0002.htm-12011294000002>> accessed 7th May 2015. This deadline was extended to November 2012 by which time it was to prove that self-regulation was working effectively. HC Deb 8th November 2012 col 993 <<http://www.publications.parliament.uk/pa/cm201213/cmhansrd/cm121108/debtext/121108-0001.htm-12110868001185>> accessed 7th May 2015

²⁵¹ Business Innovation and Skills Committee, *Consultation on a Statutory Code for Pub Companies*, (HC 2013-14, 314) at para 11, p8. N Morris, 'Vince Cable steps in to protect pub landlords from sharp practice by large pub companies' (The Telegraph, 8th January 2013) <<http://www.independent.co.uk/news/uk/home-news/vince-cable-steps-in-to-protect-pub-landlords-from-sharp-practice-by-large-pub-companies-8443283.html>> accessed 3rd July 2015

²⁵² Department for Business Innovation & Skills, *Pub Companies and tenants a Government Consultation* (22nd April 2013) at para 3.9, p12

result in “*serious hardship*”.²⁵³ The aim of the consultation was stated to be ensuring fairness to tenants whilst also safeguarding the long-term sustainability of the industry by placing reliance on ‘proportionate and targeted’ interventions.²⁵⁴ The Government’s proposals appeared to be in line with the BISC’s aforementioned aim to ensure that tied tenants are no worse off than their free-of-tie counterparts with it seeking to ensure this through the implementation of a statutory code together with an Adjudicator.²⁵⁵

5.1 A statutory code and Adjudicator

The existing industry Framework Code was to form the starting point for the statutory Code, subject to strengthening to address the principle aims of fairness and ensuring that tied tenants are no worse off than their free-of-tie counterparts.²⁵⁶ The Code would only be applicable to those pubcos which have 500 or more pubs, with the aim being to target those with market power and to exclude those smaller companies who are generally considered to act responsibly towards their tenants in light of the very few complaints received regarding them.²⁵⁷ The terms of the Code would be applicable to non-managed pubs only given that managed houses are run by employees of the pub company.²⁵⁸ The Government intended that the Code would be immediately binding and in the case of a conflict would supersede the terms of any lease or tenancy agreement.²⁵⁹ It was also proposed that the new Adjudicator should be based on the Groceries Code Adjudicator and have an arbitration and an investigative function.²⁶⁰

5.1.1 Content of the Code - The free-of-tie option

The terms of the Code were to ensure that risk and reward are shared at an appropriate level between the parties and so make sure that tied tenants are no worse off than their free-of-tie counterparts.²⁶¹ A free-of-tie option with an open market rent review had previously been suggested as a means of achieving these core principles.²⁶² The Government clarified that this is “*an option in which the tenant is subject to no purchasing*

²⁵³ Ibid at para 3.10, p12. In its consultation document it was noted that 46% of tied publicans earn below £15,000 per annum by comparison to only 23% of their free-of-tie counterparts. (Ibid at para 3.6, p12)

²⁵⁴ Ibid at para 3.8, p12. The Government provided examples of the unfair behaviour towards tenants reported to them, including large rent increase without justification, the overvaluing of additional services provided by pubcos and inaccurate statements of potential sales. (Ibid at para 3.4, p11)

²⁵⁵ Above, n.252 at para 3.12-3.13, p13

²⁵⁶ Ibid at para 4.6, p16

²⁵⁷ Ibid at para 4.11, p17

²⁵⁸ Ibid at para 4.34, p20

²⁵⁹ Ibid at para 4.15, p20

²⁶⁰ Ibid at para 4.8, p16-17

²⁶¹ Ibid at para 5.1, p23. The focus here shall be on the central issue of whether or not the Code should incorporate a free-of-tie option.

²⁶² Ibid at para 5.25, p29

obligations of any form and therefore the only sum paid to the pub company is the dry rent".²⁶³ It was however suggested that within the free-of-tie option one possibility would be for pubcos with their own brewing operations, to be allowed to require their pubs to sell only their beers, or that a certain proportion of the beers sold had to be the brewer's own but could be purchased from any source the tenant wished.²⁶⁴

5.1.2 Differing views over a mandatory free-of-tie option

In the course of its consultation the Government sought views on the inclusion of a mandatory free-of-tie option. This had the potential to be highly interventionist with the Government highlighting its concerns over such an approach.²⁶⁵ The Government noted uncertainty over the impact such an obligation could have on the market highlighting that the last significant Government intervention, namely the Beer Orders discussed in Chapter 2, had the unexpected effect of promoting the growth of pubcos and contributing to the current concerns within the industry.²⁶⁶ This was deemed to emphasise the need for proportionate measures to be adopted. The Government also highlighted the long history of beer tie agreements within the UK market and their importance in promoting the growth of small and medium sized brewers by guaranteeing them a market for their products, and assisting them in building their brands.²⁶⁷ It was thought that this could be undermined by the uncertainty associated with a mandatory free-of-tie option which could potentially accelerate pub closures.²⁶⁸ They also pointed to the buoyant craft and micro-brewing industry in the UK as an indication that the current industry structure is highly beneficial to brewers. Over one thousand British brewers were in operation, which is the highest number since the 1930s.²⁶⁹

Opposing views were expressed by tenant groups which, similarly to the BISC, highlighted that a free-of-tie option was the simplest avenue for reform as it would ultimately allow the market to decide which option is best.²⁷⁰ They also conflicted with the Government by claiming that a free-of-tie option would promote the growth of microbrewers as the majority of their sales are to free-of-tie pubs, and so an increase in their number would increase their potential market.²⁷¹ Greater consumer choice within each public house was

²⁶³ Ibid at para 5.25, p29. As discussed in Chapter 2, 'dry' rent is the property rent.

²⁶⁴ Above, n.252 at para 5.26, p29

²⁶⁵ Ibid at para 5.28, p29

²⁶⁶ Ibid at para 5.32, p31

²⁶⁷ Ibid at para 5.33, p31. This is also discussed in Chapter 2.

²⁶⁸ Above, n.252 at para 5.33, p31

²⁶⁹ Ibid at para 5.34, p31

²⁷⁰ Ibid at para 5.36, p31

²⁷¹ Ibid at para 5.36, p31

also projected as they would be free to choose the beers sold, although this was dependent on tenants choosing a wide range to sell in their public houses.²⁷²

Notwithstanding these potential benefits, brewers and pub companies were naturally keen to highlight a relatively long list of negatives associated with a free-of-tie option. These included the potential loss of economies of scale which would prevent pubcos from negotiating discounts from brewers and would reduce the efficiency of national distribution networks.²⁷³ Structural implications resulting from the absence of pubco buying power were thought to include domination of the UK market by the large international brewers who would be free to offer discounts to publicans in return for exclusivity, thereby potentially contributing to the foreclosure of the market.²⁷⁴ An erosion of the tie would also damage the partnership between the pubco and the tenant, as in the absence of being able to guarantee the right to tie a public house the incentives to promote the business of the tied publican would be lacking.²⁷⁵ It was thought that it could also cause the exit of major pubcos given the significant reliance they place on the tie as part of their business model, with the closure or sale of thousands of public houses resulting, with this uncertainty also being likely to discourage investment.²⁷⁶ Similar concerns were expressed with regard to brewing pubcos in light of their dependence on sales through their tied estates although the likelihood of this would be reduced by permitting them to require the sale of their beers through their houses, where the tenant was allowed to purchase these from any source as discussed above.²⁷⁷

5.2 Exclusion of mandatory free-of-tie option

The BISC in its response to the Government's consultation welcomed the proposals for a statutory Code and Adjudicator. While they again reiterated that they did not support the abolition of the beer tie, they were supportive of a free-of-tie option. This was due to the fact that should the tie be seen to present significant benefits to the lessee, the option would not be relied upon and the tie would continue to prevail.²⁷⁸ Further, from responses

²⁷² Ibid at para 5.36, p31

²⁷³ Ibid at para 5.37, p32

²⁷⁴ Ibid at para 5.37, p32

²⁷⁵ Ibid at para 5.37, p32

²⁷⁶ Ibid at para 5.37, p32

²⁷⁷ Ibid at para 5.37, p32

²⁷⁸ Business Innovation and Skills Committee, *Consultation on a Statutory Code for Pub Companies*, (HC 2013-14, 314) at para 31, p14

received to the Government's consultation,²⁷⁹ 67% supported a mandatory free-of-tie option and 92% supported an open market rent assessment.²⁸⁰

The Government's response to the consultation reiterated its commitment to the introduction of a statutory Code in order to ensure fairness and transparency in the industry, with all tenants being permitted to request an open market rent review should they not have had one for five years, as well as the right to take disputes before an independent Adjudicator.²⁸¹ These proposals were to be incorporated into a 'Core Code' applicable to all tied tenants.²⁸² The Government also proposed to introduce an 'Enhanced Code' applicable to all tenants of pubcos tying 500 or more public houses.²⁸³ This would incorporate provisions requiring pubcos to offer parallel tied and free-of-tie rent assessments where requested by new and existing tenants either when deciding whether to take on a pub tenancy or at the time of their tied rent review.²⁸⁴ The Government considered that this provision would achieve its core principle of allowing tied tenants to test whether or not they would be worse off than free-of-tie tenants.²⁸⁵ This was so even although the tenant would only be able to request such a review when the parties were unable to agree on the tied rent and the tenant would also be required to pay a £200 fee to the Adjudicator on doing so.²⁸⁶ This was the Government's favoured option despite the fact that only 30% of respondents were supportive of a parallel rent assessment.²⁸⁷

The Government commissioned independent analysis from London Economics on the impact of the two options namely the free-of tie option and its favoured parallel rent

²⁷⁹ Department for Business, Innovation and Skills, *Pub companies and Tenants Consultation Responses*, December 2013 at p3

²⁸⁰ HC Deb 21st January 2014, col 167

<<http://www.publications.parliament.uk/pa/cm201314/cmhansrd/cm140121/debtext/140121-0001.htm>> accessed 10th May 2015

²⁸¹ Department for Business, Innovation and Skills, *Pub Companies and Tenants Government Response to the Consultation* (June 2014) at p5

²⁸² Ibid at p5

²⁸³ Ibid at p5. As this is a devolved matter only pubs located in England and Wales would contribute to the 500 pub threshold under the Enhanced Code. (Department for Business, Innovation and Skills, *Pub Companies and Tenants Government Response to the Consultation*, June 2014 at p15) There has however been cross party support for the introduction of statutory code of practice for pubcos operating in Scotland. (Motion S4M-12348: Paul Martin, Glasgow Provan, Scottish Labour, Lodged 19th February (*Scottish Parliament*, February 2015)

<<http://www.scottish.parliament.uk/parliamentarybusiness/28877.aspx?SearchType=Advance&ReferenceNumbers=S4M-12348&ResultsPerPage=10>> accessed 5th May 2015) This will not be considered further.

²⁸⁴ Above, n.281 at p5

²⁸⁵ Ibid at p5

²⁸⁶ Ibid at p6

²⁸⁷ Ibid at p67

assessment.²⁸⁸ While it accepted that a mandatory free-of-tie option was the quickest and simplest option for ensuring that tied tenants are no worse off than their free-of-tie counterparts, it focused on the concerns noted above over the uncertainty that would be caused by such an option and its impact on the broader pub sector.²⁸⁹ The parallel rent assessment avoided the risk of unintended consequences associated with the free-of-tie option and the perceived uncertainty of whether pubs would or would not remain tied, despite concerns that such an approach was too simplistic to capture all of the variables in this complex business model.²⁹⁰ For similar reasons, the Government also vetoed the inclusion of a guest beer option as this would potentially undermine the tied model should tenants rely on it to purchase their best selling beer out-with the tie.²⁹¹

5.3 Intervention by members of the UK Parliament

Although the Government deemed the foregoing proposal to be a “*proportionate and targeted response*” it was ultimately lack luster.²⁹² The proposals failed to strike the right balance between avoiding unintended consequences, undermining the beer tie as a legitimate business model and addressing the need for change. The fact the Government had clearly misread the mood for real change and succumbed to the pressure of larger companies was evident when in June 2014 the Small Business, Enterprise and Employment Bill (2014 Bill) was introduced to Parliament.²⁹³ Part 4 made provisions for the statutory Code and the Adjudicator in line with the foregoing proposals however this was subject to amendment during a House of Commons vote in November 2014 with the surprise insertion of a new clause 2 into the Bill.²⁹⁴ Contrary to the Government’s desire to maintain the tied house system largely unchanged, Members of Parliament (MPs) rebelled

²⁸⁸ Ibid at p71. Also London Economics, *Modelling the impact of proposed policies on pubs and the pub sector A report to the Department for Business, Innovation and Skills Project reference : 008/ 1314* (December 2013). This report was greatly criticised and was considered to be very one sided, failing to take into account the views of tenants or their representative bodies. HC Deb 14th October 2014, col 60
<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141014/pm/141014s01.htm>>
accessed 7th June 2015; HC Deb 28th October 2014, col 331
<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/pm/141028s01.htm>>
accessed 11th June 2015; HL Deb 9th March 2015, col 458
<<http://www.publications.parliament.uk/pa/ld201415/ldhansrd/text/150309-0001.htm - 1503098000524>>
accessed 7th June 2015

²⁸⁹ Above, n.281 at p73-74

²⁹⁰ Ibid at p74-75

²⁹¹ Ibid at p6

²⁹² Ibid at p7. Also HC Deb 11th June 2014, col 591

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm140611/debtext/140611-0002.htm - 14061151000324>> accessed 10th May 2015

²⁹³ HL Deb 28th January 2015, GC 116

<<http://www.publications.parliament.uk/pa/ld201415/ldhansrd/text/150128-gc0001.htm - 15012858000257>>
accessed 7th June 2015

²⁹⁴ HC Deb 18th November 2014, col 195-196

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm141118/debtext/141118-0002.htm>>
accessed 11th May 2015

and voted in favour of the insertion of a ‘Market Rent Only option’, or mandatory free-of-tie obligation, for large pub-owning businesses.²⁹⁵ While the 2014 Bill was subject to further amendment following its passage through Parliament, these initial revisions set the tone for the 2014 Bill which received Royal Assent on 26th March 2015.²⁹⁶ The Small Business, Enterprise and Employment Act 2015 (the 2015 Act) is therefore a significant departure from the Government’s original proposals and its long held position on the beer tie, not to mention the EU’s acceptance of it as a legitimate business model, as discussed in Chapter 3.

6. The Small Business, Enterprise and Employment Act 2015 (the 2015 Act)

6.1 The Pubs Code

The 2015 Act makes provision for ‘the creation of a Pubs Code and Adjudicator for the regulation of dealings by pub-owning businesses with their tied pub tenants.’ Provision is made in Part 4²⁹⁷ of the Act for a statutory Pubs Code and Adjudicator in England and Wales.²⁹⁸ A large amount of detail regarding the new regulatory regime will be contained in the Pubs Code, despite the industry’s past failure to comply with such codes, as discussed above. However notwithstanding these concerns, as the Pubs Code is confined to secondary legislation, this affords greater flexibility in altering its terms in accordance with changing market conditions.²⁹⁹ The 2015 Act reiterates that the Pubs Code is to be consistent with the Government’s two main aims, namely ensuring fair and lawful dealing by pub owning businesses in relation to their tied pub tenants; and the principle that tied tenants should be no worse off than they would be if they were not subject to a product or

²⁹⁵ Ibid

²⁹⁶ HL Deb 26th March 2015, col 1590

<<http://www.publications.parliament.uk/pa/ld201415/ldhansrd/text/150326-0002.htm#15032625000607>> accessed 14th July 2015

²⁹⁷ Only Part 4 of the 2015 Act will be considered in this chapter given its relevance to the regulation of the distribution of beer in the UK.

²⁹⁸ As already noted above, at n.283, this a devolved matter. The application of Part 4 of the 2015 Act to Scotland was discussed in the House of Lords and it was acknowledged that the Scottish Parliament is considering similar intervention in Scotland. (HL Deb 28th January 2015, Col GC 163 -166 <<http://www.publications.parliament.uk/pa/ld201415/ldhansrd/text/150128-gc0001.htm - 15012858000257>> accessed 7th June 2015) CAMRA has also launched a campaign to ensure that pubco reform is brought about in Scotland. (CAMRA, ‘CAMRA launches a campaign to promote pubco reform in Scotland’ (*CAMRA*) <http://www.camra.org.uk/news/-/asset_publisher/1dUgQCmQMoVC/content/camra-launches-a-campaign-to-promote-pubco-reform-in-scotla-1> accessed 9th June 2015) This will not be considered any further here as the provisions of the 2015 Act will most likely form the basis for any subsequent reform in Scotland.

²⁹⁹ HC Deb 28th October 2014, col 305-307

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/am/141028s01.htm>> accessed 7th June 2015

service tie.³⁰⁰ It is therefore intended to support the provisions of Part 4 of 2015 Act, some of which came into force two months after the Act received Royal Assent in March and largely detail the provisions to be included in the Pubs Code.³⁰¹ The Code will be effective from May 2016.³⁰²

Whilst the 2015 Act makes provision for a Market Rent Only option, on which focus will be placed here, s.42(5) of the 2015 Act states that the Pubs Code may require pub-owning businesses to provide parallel rent assessments in relation to their tied tenants in specified circumstances.³⁰³ This is so even although it received very little backing in the Government's consultation and has been criticised as being a time consuming and complex procedure which fails to substantially alter the balance of risk and reward between the parties contrary to the intended aims of the reforms.³⁰⁴ The parallel rent assessment is proposed to increase transparency in negotiations, however there are numerous difficulties associated with its implementation including calculating the value of the special commercial or financial advantage (SCORFA) afforded to tenants, thereby undermining its usefulness.³⁰⁵

However, notwithstanding concerns over the retention of the parallel rent assessment procedure and the inability of the industry to comply with codes of practice, there are thirty two sections of the 2015 Act implementing reforms to the regulation of the UK market. Focus here shall be placed on those provisions dealing with the 'Market Rent Only option' (MRO option) given that it is the most significant challenge to the tied house system in the UK since the Beer Orders and the focus of the thesis is the distribution of beer and in particular beer tying agreements.

³⁰⁰ Section 42(3) of the 2015 Act. Product tie is defined to include beer tying obligations. It refers to a contractual obligation of a tied pub tenant that a product to be sold at the tied pub must be supplied by the landlord or a group undertaking in relation to the landlord or a nominee of either, with a service tie being the equivalent in relation to a service supplied to the tied tenant. 'Stocking requirements', which are discussed later, are specifically excluded from the product tie definition. (Section 72(1) 2015 Act)

³⁰¹ Section 164(3)(d) of the 2015 Act provides that s.42-44 (Pubs Code) and s.68-73 (Part 4: supplementary) come into force at the end of the period of 2 months beginning on the day on which the Act is passed.

³⁰² Section 42(1) of the 2015 Act provides the Secretary of State with an additional period of one year from the date the section comes into force to draft the Pubs Code and so the relevant date is May 2016. A final draft of the Code is therefore awaited. Consequently consideration here shall be limited to the provisions of the 2015 Act not the current draft of the Code.

³⁰³ Section 42(5) 2015 Act

³⁰⁴ HC Deb 16th July 2014, col 928-929,

<[http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm140716/debtext/140716-0002.htm - 14071659000001](http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm140716/debtext/140716-0002.htm-14071659000001)> accessed 7th June 2015. The Secretary of State has the power to define 'parallel rent assessment' in regulations to ensure there is flexibility in how the Pubs Code addresses this for different types of tied pub agreements. See s.72(1) 2015 Act.

³⁰⁵ HC Deb 28th October 2014, col 341- 343

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/pm/141028s01.htm>> accessed 11th June 2015

6.2 Scope of application of Part 4 of the 2015 Act and the MRO option

6.2.1 ‘Pub-owning business’, ‘tied pub’ and ‘tied pub tenant’

The scope of application of the 2015 Act and so the MRO option is largely set by the definition of three key terms, namely ‘Pub-owning business’, ‘tied pub’ and ‘tied pub tenant’.

6.2.1.1 ‘Pub-owning business’

‘Pub-owning business’ is defined in s.69(1) of the 2015 Act. This is ‘a person that in the period beginning with the day on which the Pubs Code comes into force and ending on the last day of that financial year³⁰⁶ was the landlord of 500 or more tied pubs; and is a pub owning business in any subsequent financial year, if for a period of at least 6 months in the previous financial year the person was the landlord of 500 or more tied pubs’. The application of the provisions of Part 4 of the 2015 Act is therefore restricted to those pubcos with 500 or more tied pubs. Some flexibility is however introduced into the s.69(1) threshold by s.69(8). This permits the Secretary of State to amend the threshold through the substitution of a different number of tied pubs, or a different period, from those specified thereby enabling the legislation to respond to changing market conditions. However in addition to increasing flexibility, this potentially serves to increase the uncertainty for the market with regard to the application of Part 4 of the Act, which may in turn undermine investment in the industry.³⁰⁷

6.2.1.1.1 Threshold for application

The inclusion of a threshold based on quantity is also a questionable choice given that it potentially creates a two-tier system of regulation for pubcos falling above and below this threshold. As discussed in Chapter 2, the Tied Estate Order similarly imposed a threshold of ‘more than 2,000 licensed premises’ as the basis for its application, thereby restricting it to the six largest brewers at that time.³⁰⁸ By focusing on those with over 2,000 licensed premises and using 2,000 as the cap on the number of such premises brewers could own, it had many unintended consequences some of which, namely the growth of the pubco, the 2015 Act is seeking to address. Further, while large pubcos have been the source of the

³⁰⁶ ‘Financial year’ is defined in s.72(1) as a period of 12 months beginning on 1 April and ending on 31 March.

³⁰⁷ In light of these concerns it was proposed that any change in the threshold should be confined to primary legislation. HL Deb 28th January 2015, col GC151
<<http://www.publications.parliament.uk/pa/ld201415/ldhansrd/text/150128-gc0001.htm - 15012858000257>>
accessed 7th June 2015

³⁰⁸ See Chapter 2, p36

concerns discussed in the various reports produced over the last decade, the overarching aim of the proposals was to ensure that tied tenants are no worse off than their free-of-tie counterparts, without it being suggested that the benefits of this be limited to tied tenants of the largest pubcos. While CAMRA consider that this threshold is appropriate as the leases of the larger pubcos present a greater risk to tenants,³⁰⁹ it is questionable whether or not this strikes the right balance between avoiding imposing a disproportionate burden on small brewers without undermining the intention of the reforms.³¹⁰

6.2.1.1.2 Danger of pub-owning companies evading the provisions

Furthermore, as discussed in Chapter 2, the aftermath of the Beer Orders highlighted the skill with which the UK market has been able to remodel itself in order get around restrictions imposed on it by Parliament. Consequently, a further concern associated with the adoption of the threshold requirement in s.69(1) is the ability of pub owning businesses to restructure in order to exempt their pubs and so evade the application of the provisions. These concerns are accentuated by the fact that the threshold criteria specifically refers to 500 *tied* pubs.³¹¹ Whilst the intention behind this was to remove small regional and family brewers from the scope of the provisions, during debate in the House of Lords it was correctly suggested that this threshold should cover all relationships between pubcos and their tenants, not just those based on the tied model.³¹² Limiting it in this way opens up the possibility of some pub-owning companies simply having to dispose of a single tied pub to fall below the threshold.³¹³ Further, it was considered that within the leasehold model of ownership there is generally movement between tied and non-tied pubs creating the

³⁰⁹ HC Deb 16th October 2014, col 80-81, Q172 and col 87, Q188-189 concerning CAMRA's 2013 survey of tenants' views of larger pubcos and family brewers

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141014/pm/141014s01.htm>> accessed 7th June 2015. The survey revealed that 71% of tenants of pubcos with 500 pubs compared to 49% of licensees tied to family brewers had a negative view of the beer tie agreement. While the proportion of those tied to family brewers with a negative outlook is significantly smaller than those tied to a large pubco, a significant proportion, almost half of them, have a negative view of tying arrangements as a result. This is so even although large pubcos tie a significantly higher number of pubs than family brewers causing doubt to be placed on the value of this finding

³¹⁰ Abuse of publicans by independent, small brewers was discussed in the House of Commons. HC Deb 14th October 2014, col 59 at Q129

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141014/pm/141014s01.htm>> accessed 7th June 2015. ALMR also support regulation for all. See HC Deb 16th October 2014, col 89-90, Q194

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141014/pm/141014s01.htm>> accessed 7th June 2015. Concerns over the practices of family brewers was also highlighted. HC Deb 30th October 2014, col 372

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141030/am/141030s01.htm>> accessed 11th June 2015. It was also noted in the responses received to the Government's consultation.

Above, n.281 at p25

³¹¹ Section 69(1) 2015 Act

³¹² Above, n.293 at GC 116

³¹³ Ibid at GC 116

possibility for exploitation of market power.³¹⁴ This highlights the importance of linking the two so that the 500 threshold would be applicable in such circumstances and not simply limited to tied pubs.³¹⁵ Therefore although the concerns in the reports discussed above have primarily focused on tied pubs, the threshold for determining who Part 4 of the 2015 Act applies to should be based on the size of the company as a whole, thereby requiring that all types of tenancies be taken into consideration in determining this.³¹⁶ The desire to do so is linked to the issue of market share and the possibility for anticompetitive behaviour arising out of the ownership of a substantial number of pubs.³¹⁷ Implementing generally applicable provisions would therefore potentially have been simpler and would also have avoided the possible creation of a two-tier system of regulation that is open to manipulation.³¹⁸

6.2.1.1.3 Calculating the number of pubs owned

However, notwithstanding the foregoing concerns over pub owning businesses attempting to evade the application of the Pubs Code, in calculating the number of tied pubs of which a person is the landlord, s.69(2) provides that any tied pub the landlord of which is a group undertaking in relation to that person is treated as a tied pub of which that person is a landlord.³¹⁹ Considering the collective number of pubs within a group structure in this way should limit the possibility of companies restructuring in order to avoid the application of the Pubs Code.³²⁰ However whilst the intention is to avoid pubcos devising structures that allow them to evade the provisions, it is highly unlikely that the Act could cover all possibilities as it remains to be seen how pubcos will react to the 2015 Act and so whether there are unintended consequences of the legislation. Provision is therefore made in s.69(8) to increase its flexibility.³²¹ The Secretary of State may by regulations specify the circumstances in which a person who is a group undertaking in relation to a pub owning business is to be treated as a pub owning business, as well as or instead of another person for the purposes of Part 4 of the 2015 Act. Whilst this undoubtedly increases the flexibility of the Act, there remains the possibility that such a power increases the uncertainty of the application of the provisions for pub owning businesses.

³¹⁴ Ibid at GC 119

³¹⁵ Ibid at GC 119

³¹⁶ Ibid at GC 116

³¹⁷ HC Deb 28th October 2014, col 352

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/pm/141028s01.htm>> accessed 11th June 2015

³¹⁸ Concerns over this were expressed during the Government's consultation. Above, n.281 at p24

³¹⁹ Section 69(2) 2015 Act

³²⁰ See above, n.293 at GC 132

³²¹ Section 69(8) 2015 Act

Nevertheless, a person is also considered to be a ‘pub-owning business’ where they do not satisfy the requirements of s.69(1), and so the threshold of 500 tied pubs, but are the landlord of a tied pub occupied by a tied tenant who has ‘extended protection’ in relation to that tied pub.³²² This covers those tenants who occupied a tied pub under a tenancy or licence at a time when the landlord came within the definition contained in s.69(1) and before the end of their tenancy or licence the landlord is no longer such a person due to a transfer of title or for some other reason.³²³ Consequently, the protections of the Pubs Code rightly continue for tenants when their Landlord no longer satisfies the 500 tied pub threshold. However, s.69(7) precludes the application of the MRO provisions³²⁴ and those relating to investigations by the adjudicator³²⁵ to pub-owning companies in these circumstances.

6.2.1.1.4 Loopholes in the 2015 Act - managed pubs excluded

Despite the foregoing measures to prevent pubcos restructuring and selling pubs to avoid being subject to the Code, loopholes are created in the regulatory regime by limiting the application of Part 4 of the 2015 Act to tied pubs. One notable exception from the provisions of Part 4 of the 2015 Act is managed pubs.³²⁶ As a result, pub-owning businesses of a significant size that would be expected to come within the Pubs Code do not.³²⁷ This therefore opens up the possibility of other companies taking measures such as switching from tied to managed estates of pubs in order to exempt themselves from the provisions, thereby undermining the intention of the Act.³²⁸

³²² Section 69(3) 2015 Act. However the MRO provisions contained in sections 43-45 are inapplicable to such ‘pub-owning businesses’ (s.69(7) 2015 Act).

³²³ Section 69(4) 2015 Act. This extended protection ends under the circumstances prescribed in s.69(5) namely on the earlier of the end of the tenancy or licence concerned and the conclusion of the first rent assessment of money payable in lieu of rent to be provided after the person is no longer a pub-owning business by virtue of s.69(1).

³²⁴ Section 43-45 2015 Act. As will be discussed below, this was influenced by concerns that selling pubs subject to the MRO provisions could ultimately stifle the market for the sale of such pubs.

³²⁵ Sections 53-59 2015 Act. This is due to the fact these are concerned with uncovering systemic breaches of the Code. HC Deb 24th March 2015, col 1341

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm - 15032473000004>> accessed 7th June 2015

³²⁶ Arguments were made in Parliament that managed pubs should be excluded as they are run by employees of the company who are salaried and as such are effectively running a ‘branch office’ thereby distinguishing them from tied publicans who are essentially ‘self employed small business men’ (Above, n.293 at GC 98).

³²⁷ Pubcos Mitchells & Butler and Wetherspoons are large, managed pub chains and as such do not have any tied pubs. Further, Spirit Pub Company, which at the time the 2014 Bill was passing through Parliament owned 1,200 pubs of which only 430 were on a leased model, are also precluded from its scope. See above n.317.

³²⁸ Above, n.281 at p72. Interest groups consider that the likelihood of this occurring is overstated by pubcos.

6.2.1.2 ‘Tied pub’

The 2015 Act however lays down a number of conditions to be met in order for premises to come within the definition of a ‘tied pub.’³²⁹ The conditions are contained in s.68 and include the requirement that the premises must be licensed for the retail sale of alcohol for consumption on the premises, with the sale of alcohol to the public for consumption on the premises being the, or one of the main activities carried on at the premises.³³⁰ The premises in question must also be occupied under a tenancy or license and be subject to a contractual obligation that some or all of the alcohol sold at the premises is supplied by the landlord, a person who is a group undertaking in relation to the landlord, or a nominee of either.³³¹ While these conditions will be satisfied by many pubs, the drafting of this provision is not sufficiently tight to exclude other on-trade establishments, such as restaurants, coming within the definition of a ‘tied pub’ and so being inappropriately covered by the Pubs Code.³³² The difficulty of definition has however been increased due to the growing focus on the provision of food in many pubs with it being deemed necessary for the Secretary of State to have the authority to grant exemptions from the Pubs Code in order to ensure its proper application.³³³ However, whilst it is important to ensure the proper application of the Pubs Code, the power to grant exemptions under s.71 also potentially opens up the possibility of pubcos abusing this provision by seeking to comply with its terms, for example through the adoption of the franchise model, in order to have their premises exempted from the Pubs Code.³³⁴ The s.71 power therefore has to be used with caution in order to prevent the Pubs Code being undermined through the creation of exceptions and so loopholes.

³²⁹ Section 68 2015 Act

³³⁰ Section 68 (2)-(3) 2015 Act

³³¹ Section 68 (4)-(5) 2015 Act

³³² The British Franchise Association raised concerns over this during the course of early debates. HC Deb 30th October 2014, col 367

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141030/am/141030s01.htm>> accessed 11th June 2015

³³³ HC Deb 18th November 2014, col 147

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm141118/debtext/141118-0001.htm - 14111843000002>> accessed 11th June 2015. This power is granted under s.71 2015 Act.

³³⁴ This danger was also recognised in the House of Lords (see above, n. 293 at GC 152-153). The issue of whether or not franchises would be included in Part 4 was frequently raised during the course of the 2014 Bill’s passage through Parliament. Pub franchise agreements based on a share of turnover rather than a tied tenant were considered to better align the interests of the parties. The decision was later taken to exempt ‘genuine’ franchise agreements from the Pubs Code under the powers granted by s.71 2015 Act. The definition of a ‘genuine franchise’ is to be consulted on later. This was despite the fact franchises share many of the characteristics of a traditional tied pub and so aspects of the relationship have the potential to lead to unfairness. This creates an additional loophole in the 2015 Act which could potentially be exploited by pubcos. Above, n.293 at GC 160 and HC Deb 24th March 2015, col 1344.

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm - 15032473000004>> accessed 7th June 2015

6.2.1.2.1 Exclusion of ‘stocking requirements’ from definition

Section 68(5) of the 2015 Act also removes from the definition of ‘tied pub’, premises that are subject to a contractual obligation amounting to a ‘stocking requirement’.³³⁵ Section 68(7) provides that a contractual obligation is a stocking requirement if, firstly, it concerns only beer and or cider produced by the landlord or by a person who is a group undertaking in relation to the landlord.³³⁶ Secondly, the tied pub tenant is not required to source the beer or cider from any particular supplier,³³⁷ and thirdly, the tied pub tenant is not precluded from selling on the premises beer or cider produced by another supplier.³³⁸ The intention of this provision is to exclude from Part 4 pubs owned by brewing pubcos.

During parliamentary debates, it was deemed logical for such pubcos to be allowed to require their tenants stock their own brands of beer and cider with it being suggested that precluding this would cut off approximately 30% of their market.³³⁹ These provisions were therefore considered to be necessary to safeguard their existence. As s.68 does not require the tenant to source beer or cider from a particular supplier, on the face of it, it appears to strike a balance between the brewer having to compete for the tenant’s business and ensure they offer the best price for the product, whilst allowing the brewer to benefit from the protection of requiring their products are sold in their own pubs.³⁴⁰ CAMRA have declared their support for this exclusion of stocking requirements from the provisions of the Act as they are a means of ensuring that brewing pubcos are able to continue to distribute their brands.³⁴¹ However, whilst it is undoubtedly important that steps are taken to protect smaller and regional brewers whose survival is dependent on selling their brands through their own pubs, it is suggested that brewers could also take steps to ensure that they are the only source from which their beers can be purchased, thereby circumventing the intention of these provisions and undermining the protection it affords to tenants. It will therefore remain to be seen whether or not such actions would be effectively addressed by the Adjudicator.³⁴²

³³⁵ Section 68(6) 2015 Act

³³⁶ Section 68(7)(a) 2015 Act

³³⁷ Section 68(7)(b) 2015 Act

³³⁸ Section 68(7)(c) 2015 Act

³³⁹ Above, n.293 at GC 101-102

³⁴⁰ Ibid at GC 102

³⁴¹ Ibid at GC 123

³⁴² HC Deb 24th March 2015, col 1343

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm-15032473000004>> accessed 7th June 2015

6.2.1.3 'Tied pub tenant'

'Tied pub tenant' is defined in s.70(1)(a) as a person 'who is the tenant or licensee of a tied pub', or under s.70(1)(b) 'who is a party to negotiations relating to a prospective tenancy of or licence to occupy premises which are, or on completion of the negotiations are expected to be, a tied pub.' Concerns were expressed in Parliament that this provision was too widely drafted and so had the potential to extend the benefit of the Pubs Code to those who were in the very early stages of negotiations with pub owning companies.³⁴³ However, affording protection from an early stage and so before negotiations are concluded between the parties, was correctly deemed to be required in order to help redress the imbalance between the parties. This ensures that potential tenants have access to the necessary and correct information in order to make an informed decision and so reduces the possibility of them entering into a disadvantageous contract.³⁴⁴

6.3 The MRO option

Section 43 of the 2015 Act is intended to achieve the Government's aim of ensuring that tied tenants are no worse off than those who are free of a product or service tie. It is an extensive provision and provides for the MRO option in the Pubs Code. Section 43(1) states that the 'Pub Code must require pub-owning businesses to offer their tied pub tenants, falling within s.70(1)(a), namely existing tenants of the business, a MRO option in specified circumstances.' Prospective tenants are therefore precluded from the MRO option. The intention of Parliament was that they could request a parallel rent assessment under the Pubs Code. This is so, despite the numerous concerns and criticisms levied at this discussed above, which cast doubt on its ability to afford a significant degree of transparency to prospective tenants prior to entering into a tenancy agreement.³⁴⁵ This subsequently reduces the scope for this provision to achieve the Government's much discussed aims of ensuring fair and lawful dealing and ensuring that tied tenants are no worse off than their free-of-tie counterparts.

³⁴³ HC Deb 28th October 2014, col 358-359

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/pm/141028s01.htm>> accessed 11th June 2015

³⁴⁴ HC Deb 30th October 2014, col 378

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141030/am/141030s01.htm>> accessed 11th June 2015

³⁴⁵ Above, n.293 at GC 134 and HC Deb 24th March 2015, col 1342

<[http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm - 15032473000004](http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm-15032473000004)> accessed 7th June 2015

6.3.1 Definition of MRO option

Section 43(2) defines ‘market rent only option’ to mean the option for the tied pub tenant to occupy the tied pub under a tenancy or licence which is MRO compliant and to pay in respect of that occupation ‘such rent as may be agreed between the pub-owning business and the tied pub tenant in accordance with the MRO procedure,³⁴⁶ or failing such agreement, the market rent’.³⁴⁷ Consequently, in the event the tenant opts to accept the MRO offer, their occupation of the premises must be on a basis which is MRO compliant. A tenancy or licence is MRO compliant if, ‘taken together with any other contractual agreement between the tied pub tenant and the pub owning business in respect of that tenancy or licence it contains the terms and conditions as may be required by virtue of s.43(5)(a) and so those specified by the Pubs Code as being required to be contained in a tenancy or licence for it to be MRO compliant,³⁴⁸ does not contain any product or service tie except in respect of insurance for the tied pub, does not contain any unreasonable terms or conditions, and is not a tenancy at will.’³⁴⁹ Consequently, s.43 frees the tenant or licensee of any ties to the pubco and obliges the tenant to pay to the landlord only the market rent. Section 43 therefore eradicates the obligation on the tied tenant to pay ‘wet rent’ as was customary under a traditional tied tenancy, discussed in Chapter 2. It ensures tied tenants are no worse off than their free-of-tie counterparts by offering them the option to accept being ‘market rent only’. However, the counter effect of this is that the tenant is no longer entitled to any of the SCORFA³⁵⁰ from which they should have benefitted under the terms of their tied agreement. The process to be followed by the pub owning company in calculating this however requires to be clarified under the Pubs Code in order to avoid its abuse.³⁵¹

³⁴⁶ This will be discussed when considering s.44 of the 2015 Act

³⁴⁷ Market rent is defined as ‘the estimated rent which it would be reasonable to pay in respect of that occupation on the assumption that the tenancy or licence is entered into on the date on which the determination of the estimated rent is made, in an arm’s length transaction, after proper marketing, and between parties who acted knowledgeably, prudently and willingly, and Condition B in s.68 continues to be met, and so the main, or one of the main activities carried on at the premises is the retail sale of alcohol to members of the public for consumption on the premises.’ (Section 43(10) 2015 Act)

³⁴⁸ Section 43(5) 2015 Act

³⁴⁹ Section 43(4)(a) and (b) 2015 Act. ‘Tenancy’ is widely defined in Part 4 of the 2015 Act. Section 70(2) defines this as ‘a tenancy created either immediately or derivatively out of the freehold, whether by lease or sublease, by an agreement for a lease of sublease, by a tenancy agreement or a tenancy sub-lease agreement or in pursuance of a provision of, or made under an Act, and includes a tenancy at will.’ Tenancies at will arise when there is a sudden requirement for a short-term tenancy, such as an emergency. Their inclusion in the 2015 Act was to avoid permitting rolling shorter-tenancies to undermine the Code and so create a loophole. HC Deb 30th October 2014, col 379

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141030/am/141030s01.htm>> accessed 11th June 2015

³⁵⁰ See Chapter 3

³⁵¹ Above, n.293 at GC 128

6.3.2 Circumstances under which MRO option is to be offered

As noted above, s.43(1) requires the offer of the MRO option in ‘certain circumstances’ which will be further specified in the Pubs Code, however s.43(6) requires the Pubs Code to include provision for this in connection with certain events. These are the renewal³⁵² of any of the pub arrangements;³⁵³ or a rent assessment or assessment of money payable by the tenant in lieu of rent.³⁵⁴ They also include a significant increase in the price at which any product or service which is subject to a product or service tie is supplied to the pub tenant where the increase was not ‘reasonably foreseeable’ when the tenancy was granted or when a rent assessment or assessment of money payable in lieu of rent was last concluded,³⁵⁵ or after a ‘trigger event’.³⁵⁶

S.43 therefore details numerous points at which the pub-owning company must offer to the tenant the MRO option. However some of the terms relied on are subjective and so are lacking in certainty. This makes them potential sources of contention between the pubco and their tenants or lessees and may in turn prompt referrals to the Adjudicator, stalling the MRO option. ‘Significant increase’ for example is a very general term³⁵⁷ which is open to interpretation, and fails to provide the tenant with a clear basis on which they can expect their pubco to offer them the MRO option. Clarity is essential if the Pubs Code is to ensure fairness between the parties and so additional detail should be provided in the Code.³⁵⁸ ‘Reasonably foreseeable’ is a similarly subjective term that prompts the same concerns.³⁵⁹ Further, as the offer of MRO is to be made at the aforementioned points, in addition to the tenant lacking certainty as to whether or not the conditions of s.43 are satisfied, by linking the MRO offer to renewal of the pub arrangements or rent assessments they may have to wait several years until this offer will be made. This therefore fails to provide an immediate solution for tied tenants.

³⁵² Section 43(7) clarifies that the Pubs Code will specify what renewal means with regard to a tenancy or a licence.

³⁵³ This is defined in s.43(8) as ‘the tenancy or licence under which the tied pub is occupied, and any other contractual agreement which contains an obligation by virtue of which Condition D of s.68 is met in relation to the premises, namely the tying obligation in respect of alcohol sold and the premises.’

³⁵⁴ Section 43(6)(a) 2015 Act. This is intended to cover the situation where the tenant’s payments are linked to the pub’s turnover as opposed to a fixed rent, in which case there may be an assessment of any money payable in lieu of rent, for example under some franchise agreements. See Explanatory Notes, Small Business, Employment and Enterprise Act 2015 at para 285, p47.

³⁵⁵ Section 43(6)(c) 2015 Act

³⁵⁶ Section 43(6)(d) 2015 Act

³⁵⁷ Above, n.293 at GC 103

³⁵⁸ Ibid at GC 131

³⁵⁹ Ibid at GC 124

Section 43(6) also requires the Pubs Code make provision for the offer of the MRO option ‘after a trigger event has occurred’. ‘Trigger events’ in relation to tied pub tenants is defined in s.43(9) of the 2015 Act as ‘an event which is beyond the control of the tied pub tenant, was not reasonably foreseeable,³⁶⁰ has a significant impact on the level of trade that could reasonably be expected to be achieved at the tied pub, or is of a description specified in the Pubs Code’. The intention is therefore to capture unfair price increases and so addresses the imbalance in the relationship between the parties. However the drafting of this provision is also subjective through the inclusion of general terms such as ‘reasonably foreseeable’ and ‘significant’ and will require clarification in the Code. It is also notable that the sale of the premises does not prompt the offer of the MRO option. This was the subject of Parliament debate.³⁶¹ Whilst there was concern to afford continuing protection to the tenant in the event of the sale of the premises to a party who was not subject to the Code, it was considered that making the transfer of title a trigger point for the MRO option would stifle the pub sales market.³⁶² Whilst this may be the case, its exclusion also presents the danger that the sale of the premises may be used as a means get around the legislation.³⁶³

6.4 MRO option: Procedure

Section 44 of the 2015 Act outlines the procedure to be followed when the MRO option is exercised, and will be detailed in the Pubs Code which will also confer functions on the Adjudicator in this regard.³⁶⁴ This procedure essentially consists of two-stages. Firstly the tied pub tenant will give the pub owning business notice that they consider that they are required to offer the tenant a MRO option and that they wish to receive such an offer.³⁶⁵ The Code will specify a reasonable period, ‘the negotiation period’, during which the pub owning business and the tied tenant will seek to agree the rent to be payable in respect of the tied pub tenant’s occupation of the premises.³⁶⁶ At the end of the negotiation period, should the parties not have reached agreement, provision may be made for the appointment of an ‘independent assessor’ to determine the market rent of the premises concerned.³⁶⁷

³⁶⁰ As mentioned under s.43(6)(c) above

³⁶¹ Above, n.293 at GC 128-129

³⁶² Ibid at GC 125

³⁶³ Similar concerns were raised in connection with the administration of the pub-owning business. Above, n.293 at GC 119. Also HC Deb 24th March 2015, col 1350

<[http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm - 15032473000004](http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm150324/debtext/150324-0002.htm-15032473000004)> accessed 7th June 2015

³⁶⁴ Section 44(1) 2015 Act

³⁶⁵ Section 44(2)(a) 2015 Act

³⁶⁶ Section 44(2)(b) 2015 Act

³⁶⁷ Section 44(2)(c) 2015 Act

The Code may require the appointment of the independent assessor to be made by the parties acting jointly or should they fail to reach agreement, by the Adjudicator.³⁶⁸

Whilst the procedure outlined appears to be reasonable, it will be essential to the success of the MRO option that the independent assessor is truly independent in order to ensure that fairness and balance between the parties is reflected in the outcome. The Pubs Code may set the criteria to be met by the person appointed as an independent assessor and require that they determine the market rent within a specified reasonable period and in accordance with the provision of documents specified in the Pubs Code.³⁶⁹ ‘Reasonable period’ will have to be elaborated on in the Pubs Code in order to avoid the process becoming unnecessarily protracted. The Code may however require that the tenancy, licence under which the tied pub is occupied, or any other arrangement in connection with the tenancy or licence, continue to have effect until the MRO procedure is completed,³⁷⁰ regardless of whether or not the agreement would or could cease to have effect before that time.³⁷¹ Nevertheless, the effectiveness of the MRO option will be dependent on the procedure working efficiently and only time will tell if the one outlined in the 2015 Act will be sufficient to achieve this.

6.5 MRO option: Disputes

Section 45 of the 2015 Act enables the Secretary of State by Regulations to confer functions on the Adjudicator to resolve disputes relating to the offer of the MRO option.³⁷² It is submitted that these will need to be comprehensive and effective if the Code is not to be undermined by the actions of pubcos, given their past disdain for complying with the terms of such Codes of practice. Section 45(2) provides that the Regulation may make provision covering disputes regarding whether the circumstances are such that the pub-owning business is required to offer a tied pub tenant a market rent only option; whether a proposed tenancy is MRO compliant; whether a determination of the market rent of a tenancy or licence made by an independent assessor has been made in accordance with the Pubs Code; or whether any other requirement of the MRO procedure has been complied with.³⁷³ A further safeguard is provided by s.47 which states that the terms of an agreement between a pub-owning business and a tied pub tenant are void to the extent that they

³⁶⁸ Section 44(2)(d) 2015 Act

³⁶⁹ Section 44(2)(e)-(h) 2015 Act

³⁷⁰ Section 44(4) 2015 Act states that the Pubs Code may specify the circumstances under which the MRO procedure is treated as having come to an end.

³⁷¹ Section 44(3) 2015 Act

³⁷² Section 45(1) 2015 Act

³⁷³ Section 45(2) 2015 Act

purport to prevent the tenant from referring a dispute to the Adjudicator for arbitration in accordance with s.45 or s.48 of the 2015 Act or penalises the tenant for making such a referral.³⁷⁴ This is so regardless of whether those agreements were entered into before the provisions of the 2015 Act came into effect.³⁷⁵ However, similarly to the MRO procedure discussed earlier, it will be essential for the Pubs Code to ensure that the dispute resolution procedure works efficiently and effectively in order to prevent the process being protracted and the intentions of the Act undermined.

6.6 The UK beer market following the 2015 Act

The foregoing reforms have been introduced after a decade of Business Select Committees and pressure groups investigating and reporting on the UK market, as well as the most recent Government consultation discussed above. Despite the fact there has not been a sea change in the market concerns addressed by this reporting, substantive reform of the regulation of the UK market is only now being implemented. This suggests that reform should have occurred sooner and also should not have been left to rebel MPs to bring about in a hurried fashion.

While the reforms contained in the 2015 Act again place a significant amount of reliance on a Pubs Code, despite the industry's past failings in complying with such codes, these reforms are the most radical since the Beer Orders due to the inclusion of the MRO option. As discussed in Chapter 2, the beer tie is interwoven into the structure of the UK beer market and has played an integral role in shaping it. The MRO option however attempts to significantly weaken its operation in the UK although it falls short of severing the tie in all circumstances. The MRO offer is limited to those tied tenants of pub owning companies meeting the threshold requirements of the Act, leaving the rest of the market free to rely on the tie.

While the 2015 Act is assumed to affect only six companies, two of which are brewing pubcos, it cannot be predicted with absolute accuracy how the market will react to the MRO option.³⁷⁶ Although it is clearly more effective than the parallel rent assessment option in achieving the Government's fundamental principle that a tied tenant should be no

³⁷⁴ Section 47(4) 2015 Act. Section 48 is concerned with the referral for arbitration by tied pub tenants. While the arbitration provisions of the 2015 Act are of importance they will not be considered further here.

³⁷⁵ Section 47(6) 2015 Act

³⁷⁶ Above, n.293 at GC 97-98

worse off than their free-of-tie counterparts³⁷⁷ as it is open to the market to determine what option is best, past interventions have proven that their potential implications may serve to worsen the problems they seek to address.³⁷⁸ Similarly to the Beer Orders, the MRO provisions of Part 4 of the 2015 Act are a significant intervention in the market and as they are only available to tied tenants of pub owning businesses satisfying the threshold requirements of the 2015 Act are likely to produce a two-tier system of regulation of the UK market. Further, many of the provisions of the 2015 Act are potentially open to manipulation by pubcos and create loopholes in the regulatory regime thereby increasing the likelihood of unintended consequences.

During Parliamentary debates on the 2015 Act some of the concerns raised by the Government over the potential consequences of offering a MRO option during its consultation discussed above were justifiably reiterated. These included concerns that pubcos are motivated to increase beer volumes sold through their pubs and invest capital to support this. In the event the tie is prohibited, pubcos will likely focus almost entirely on the property aspect of their businesses and so remove any support provided to tenants whilst increasing property rents, thereby prompting the closure and sale of many pubs.³⁷⁹ It was also acknowledged that the MRO option could have knock-on effects for others in the market,³⁸⁰ including potential implications for family brewers who supply their products through the pubcos' retail chains and distribution networks.

However, the reporting on the market over the last decade has shown that the beer tie as currently operated in the UK requires to be restricted in order to address the many on-going anticompetitive issues surrounding its operation. Whilst subject to criticism and concerns, it was stated in Parliament that the introduction of the MRO option is intended to promote 'free and fair' competition in the market.³⁸¹ By loosening the pubco's grip on the UK market it has the potential to increase competition by permitting certain tied publicans to source supplies on the open market and to be placed on a more level playing field with their free-of-tie counterparts. It also increases the likelihood of certain tied publicans being able to respond to consumer demand for greater choice, by not being restricted to the sale

³⁷⁷ Essentially this means that the tenant should not be worse off as a result of being in the tied agreement and so their projected profit should be equal to or greater than that projected under a free-of-tie scenario. HC Deb 28th October 2014, col 338

<<http://www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/141028/pm/141028s01.htm>>
accessed 11th June 2015

³⁷⁸ Above, n.293 at GC 91

³⁷⁹ Above, n.293 at GC 101

³⁸⁰ HC Deb 18th November 2014, col 184

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm141118/debtext/141118-0002.htm>>
accessed 11th June 2015

³⁸¹ Above, n.293 at GC 118

of pubco approved brands in their pubs, whilst also potentially improving smaller brewers' access to tied local pubs, thereby reducing barriers to entry and market foreclosure.³⁸²

Whilst the foregoing are undoubtedly positive developments for the industry, they are limited only to qualifying tied pubs, and as discussed above, there are many concerns over the provisions of Part 4 of the 2015 Act. Furthermore, the UK market has proven itself to be particularly difficult to regulate given the powerful and resourceful players involved as well as the complexity of the relationships between them, which have their roots in the historical tied house system. The Beer Orders and failed self-regulatory attempts are testament to this. Consequently reform of the regulation of the UK beer market is not an entirely straightforward matter. It therefore remains to be seen whether Part 4 of the 2015 Act will increase market forces and the level of competition in the UK market, or whether it is effectively a backward step in its regulation given the significant potential for it to be overshadowed by unforeseen developments as have come to be synonymous with the Beer Orders of the late 1980s.

7. Conclusion

When the UK acceded to the EU in 1972, the benefits of exclusive purchasing agreements such as beer tying agreements were recognised through the offer of block exemption to these. The EU was keen to promote measures that enhanced distribution, and subsequently integration within the single market, while market integration was not of concern to the UK Government. The beer tie has therefore long been accepted as a legitimate business model in the EU, with this acceptance coming to influence the approach of the UK Government. The UK courts however initially struggled with the enforcement of the EU competition law provisions although latterly the relationship between EU and national law has developed, including the harmonisation of the two legal regimes and so the provisions applicable to beer tying agreements.

Notwithstanding the EU's acceptance of the beer tie as a legitimate business model and the Europeanisation of national law as well as the OFT's decision in 2000 that the UK market was sufficiently competitive for the Beer Orders to be revoked, concerns over the level and impact of the concentration of public house ownership in the UK, and the extensive use of beer tying agreements persisted. These concerns resulted in a decade of on-going investigation and reporting on the UK market however no substantive reform of the

³⁸² HC Deb 18th November 2014 col 191

<<http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm141118/debtext/141118-0002.htm>>
accessed 17th July 2015

regulation of the market was implemented during this time. The unforeseen consequences of the Beer Orders, discussed in Chapter 2, appeared to have had a chilling effect on further intervention in the market, with many of the reports produced shying away from suggesting similar market interventions in light of their potentially unforeseen consequences. Over this period, the OFT frequently deferred to the EU's on-going acceptance of the beer tie as a legitimate business model in order to avoid intervening in the market and so resisted strong pressure from the BISC and CAMRA, amongst others, to further investigate the operation of the beer tie in the UK. This ultimately impacted on the Government's position on the on-going concerns being raised, with it tending to follow the OFT's lead with regard to proposed interventions. As a result in 2011 the Government mistakenly opted to perpetuate self-regulation as opposed to statutory regulation of the market even although it had clearly failed on prior attempts.

Consequently the 2015 Act and the inclusion of the MRO option is the first attempt at substantive reform of regulation of the UK market since the Beer Orders. While the offer of the MRO option was contrary to the Government's clear preference to preclude this from any regulatory reform and was brought about by unexpected amendments to the Government's 2014 Bill, it is suggested that reform of some form should have occurred sooner. The terms of the reporting in relation to the UK market has not altered significantly in the last few years suggesting that the delay in doing so was unnecessary. There are however numerous issues regarding the provisions of 2015 Act and the implementation of the MRO option, which whilst stopping short of severing the beer tie entirely, significantly weakens its operation in the UK beer market. The lessons learned from the Beer Orders is that such market interventions may worsen the problems they seek to address. As discussed in Chapter 2, the beer tie is deeply integrated in the structure of the UK beer market and is a tradition that can be traced back almost to its inception. The Beer Orders and failed attempts at self-regulation have shown that the UK beer market is a difficult market to regulate given the powerful and resourceful players involved and the complexity of the relationships between them which have their roots in the archaic tied house system. Consequently whilst reporting on the market over the past decade has shown that the beer tie as currently operated in the UK requires to be restricted in order to address many of the anticompetitive issues surrounding its operation, this is not entirely straightforward. It remains to be seen whether or not the 2015 Act delivers any potential benefits or if it will be overshadowed by potentially unforeseen consequences as predicted. It is therefore not definitive whether the MRO option is the best option for reform.

In order to determine whether there is a more appropriate way to reform the regulation of the distribution of beer in the UK than that offered by the 2015 Act, consideration will now be had to the approach adopted towards the beer tie in other selected geographical markets. This will make it possible to ascertain whether any guidance can be gleaned on how best to reform the UK beer tie and in doing so, determine whether it is a legitimate business model in these jurisdictions, in the absence of the overriding goals and objectives that have informed the EU's position, and subsequently impacted on the UK's acceptance of the tie.

Chapter 5 - A Selective Comparison of Non-UK Brewing Markets

The preceding chapter analysed how the UK Government has regulated the beer tie noting the influence exerted by the EU since the UK's accession in 1973. In doing so the concerns expressed over the use of the beer tie following the OFT's decision in 2000 to revoke the Beer Orders, up to the present day have been considered along with the Government's response. This included the provisions of the Small Business, Enterprise and Employment Act 2015 (2015 Act) which introduces a Market Rent Only (MRO) option for tied tenants of pub owning businesses, which will potentially significantly weaken the operation of beer tying agreements in the UK. This chapter now considers by way of comparison with the US, Australian and Belgian beer markets whether any lessons may be learnt from the selected non-UK markets when making recommendations for the future reform of beer distribution in the UK.

The chapter first notes the potential limitations of international comparisons. It emphasises that the intention of the chapter is not a simple exportation of another legal regime into the UK. Rather it is the consideration on a case study basis of the impact of the approach towards vertical integration within selected non-UK markets (Subsection 1). It then focuses on the United States' (US) approach to the distribution of beer highlighting the impact on the market of outlawing vertical integration (Subsection 2). The chapter then considers the effect of the Australian approach to beer distribution noting that exclusive dealing is generally prohibited under the Australian antitrust provisions (Subsection 3). Finally the approach to the distribution of beer in Belgium, which is considered to have one of the most diversified beer markets in the world, will be considered (Subsection 4).

1. Potential limitations on International Comparisons

Before considering how the US, Australia and Belgium have dealt with the distribution of beer it is necessary to consider the limitations of such comparison. As Gourvish notes there are three limiting factors to the simple 'theoretical exposition of the development of brewing production and retailing'.¹ These are the impact of government regulations, especially the approach towards vertical integration, mergers and taxation; the behaviour of

¹ T.R. Gourvish, 'Economics of brewing, theory and practice: concentration and technological change in the USA, UK and West Germany' (1994) 32(1) Bus Econ Hist 253 at 253

firms themselves; and differing consumer preferences.² These factors all influence the achievement of scale economies and high concentration.³ However, as already stated above, the intention of the chapter is not a simple exportation of another legal regime into the UK. Rather, it seeks to consider the impact of the approach towards vertical integration within other jurisdictions to reveal the effect of their policies in shaping the market structure and any resulting implications. For these reasons, the selected geographical markets will be used as case studies of the different approaches that can be adopted in dealing with the distribution of beer. Focus will be placed on the US as one of the largest and most established brewing industries to examine the impact of a long-term prohibition on the beer tie. Australia will also be considered as it is a Commonwealth country and a major beer producer that has more recently taken steps to outlaw the tie in order to address the networks of tied houses owned by some of the country's most powerful brewers. Finally the Belgian beer market will be reviewed. By virtue of also being a Member State of the European Union (EU) it is subject to a very similar competition law regime to the UK, although it is considered to be the most diversified beer market in Europe.

2. The US beer market

The US beer market is one of the largest and most established in the world. The history of brewing in the US dates back to the early communities established by English and Dutch settlers in the 17th Century.⁴ Brewing was a local industry with local products being sold in local taverns, or brewed at home.⁵ By the 20th Century it was one of the leading manufacturing industries in America with the US coming to be one of the world's largest beer markets in modern times.⁶

2.1 A brief overview of the historical development of the US beer market and how the beer tie became an illegitimate business model

The future form of the US industry was largely shaped by Prohibition in the 20th Century. This resulted in the introduction of the '3-tier system' of producing, distributing and

² Ibid at p253-254

³ Ibid at p254

⁴ M.H. Stack, 'Concise History of America's brewing Industry' (*The Economic History Association*, 4th July 2003) <<http://eh.net/encyclopedia/a-concise-history-of-americas-brewing-industry/>> accessed 3rd July 2015

⁵ B Asher 'Global beer: the road to monopoly' at p4 (*The American Antitrust Institute*, September 2012) <[http://www.antitrustinstitute.org/sites/default/files/Global Beer Road to Monopoly_0.pdf](http://www.antitrustinstitute.org/sites/default/files/Global%20Beer%20Road%20to%20Monopoly_0.pdf)> accessed 2nd March 2015)

⁶ Above, n.4. The US was only eclipsed by China as the world's largest beer producer in 2003. See Deloitte, 'Profitable growth and value in the beer industry A view from Deloitte and SAP' at p1 (*Deloitte*) <[https://www.deloitte.com/assets/Dcom-Venezuela/Local Assets/Documents/White Paper_Beer%281%29%282%29.pdf](https://www.deloitte.com/assets/Dcom-Venezuela/Local%20Assets/Documents/White%20Paper_Beer%281%29%282%29.pdf)> accessed 2nd March

retailing alcohol. Following the repeal of Prohibition, brewery ownership of retail outlets was prohibited in the US.⁷

2.1.1 Prohibition and the '3-tier' system

Prohibition was largely encouraged by the increasingly powerful temperance movement. In 1919 this prompted the 18th Amendment to the US Constitution, which in conjunction with the National Prohibition Act of 1919, commonly known as the Volstead Act, outlawed the production and distribution of any beverages with more than half of one percent alcohol.⁸ These measures naturally impacted on the brewing industry, and saw brewers divest themselves of the saloons they owned or controlled. These were the primary retail outlets for alcohol, with draft beer accounting for most beer sold at that time.⁹

As Tamayo notes, in the early 20th Century beer had increased in popularity amongst Americans, prompting a corresponding increase in the number of breweries in operation with fierce competition prevailing in the beer market.¹⁰ Brewers were eager to secure guaranteed outlets for their products with this being offered by saloons, the precursor to modern day bars.¹¹ American brewers, in-keeping with their UK counterparts had, amongst others, provided furnishings, paid licence fees or provided loans on the condition that saloons carry only their brands.¹² However there were concerns that these tied house arrangements also encouraged increased alcohol consumption, as retailers were required to meet quotas causing them to encourage increased consumption by customers.¹³ The tied house system therefore soon came to be one of the principal drivers behind Prohibition with the 3-tier system being imposed to prevent this pre-Prohibition practice.¹⁴ As Tamayo notes the primary impetus for temperance was “*a societal perception of rampant public drunkenness and its attendant ills...*”¹⁵ Focus was placed squarely on saloons. In the absence of wholesalers, these were subject to significant influence from brewers.¹⁶ Tamayo also highlights that brewers’ ignorance of saloonkeepers’ involvement in illicit

⁷ Monopolies and Mergers Commission, *The Supply of Beer A Report on the supply of beer for retail sale in the United Kingdom* (Cm651, 1989) at para 8, p312

⁸ Above, n.4 at p2

⁹ The remaining beer supplies were distributed directly to homes in returnable bottles. See above, n.7 at para 15, p314

¹⁰ A Tamayo, ‘What’s brewing in the old north state: an analysis of the beer distribution laws regulating North Carolina’s craft breweries’ (2010) 88 N.C.L. Rev. 2198 at 2207

¹¹ Ibid at p2207

¹² S.L. Martin, ‘Wine wars – consumers and mom-and-pop wineries v. big business wholesalers: A citizen United Example’ (2011) (21) Kan. J.L. & Pub. Pol’y 1 at p4

¹³ Ibid at p4

¹⁴ Above, n.10 at p2207

¹⁵ Ibid at p2207-2208

¹⁶ Ibid at p2008

lines of business to boost their own profits resulted in the Prohibition movement gaining public support.¹⁷ Fourteen years of Prohibition resulted in some breweries surviving by producing low alcohol beer and soft drinks.¹⁸ The Prohibition regime however eventually ended in failure in 1933 following an increase in organised crime and general disregard for the law.¹⁹

The 21st Amendment to the US Constitution repealed the Prohibition amendment and was only passed as it afforded each State considerable autonomy in the regulation of alcohol.²⁰ Section 2 of the Amendment provides that “[t]he transportation or importation into any State, Territory or Possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited”.²¹ The Supreme Court has held that this provides individual States with a virtual monopoly in structuring the alcohol distribution system within their jurisdiction.²² As a result, numerous provisions have been introduced at the Federal and State level to control the production, distribution and sale of alcohol, including beer, with the intention being to avoid a repeat of the pre-Prohibition problems discussed above.²³ The National Industry Recovery Act (NIRA) Brewers Code was adopted and in 1935 the Federal Alcohol Administration Act (FAAA) came into effect.²⁴ This includes amongst its aims, checking individuals entering the industry to ‘keep out undesirable elements,’ and the prevention of anticompetitive practices.²⁵ Federal law did not demand that individual States had to implement the 3-tier system. However, Tamayo notes that the FAAA prompted this by prohibiting retailers from entering into tied house agreements with suppliers and wholesalers; by outlawing the practice of retailers acquiring supplies of alcohol exclusively from one source; and by

¹⁷ Ibid at p2208

¹⁸ Above, n.5 at p5

¹⁹ Above, n.10 at p2209

²⁰ Above, n.7 at para 15, p315

²¹ Amendment XXI ‘Repeal of Prohibition’ passed by Congress February 20th 1933 (*National Constitution Center*) <<http://constitutioncenter.org/constitution/the-amendments/amendment-21-amendment-18-repealed>> accessed 2nd March 2015. See also above, n.10 at p2206

²² Above, n.10 at p2206

²³ J.C. Cooper and J.D. Wright, ‘Alcohol, antitrust, and the 21st Amendment: An Empirical Examination of Post and Hold Laws’ (2012) 32 Int’l Rev.L & Econ. 379 at p379. Also above, n.7 at para 15, p315.

²⁴ The NIRA was passed in 1933 to permit the President to regulate industry to increase prices and stimulate economic recovery following deflation. To deal with issues of competition, monopoly and under employment, the National Recovery Agency (NRA) established by the NIRA increased the role of trade associations in the economy. (See A Mittelman, *Brewing Battles a History of American Beer* (United States, Algora Publishing, 2008) at p100.) The NRA made each industry write a code with their ultimate adoption being decided by the Federal Government (ibid at p102). Brewers had a pre-existing trade association which drafted their code (ibid at p103). The FAAA remains in force in part including Title 27, Chapter 8, Subchapter I s.205 on unfair competition and unlawful practices (‘United States Code’ (*Office of the Law Revision Counsel*)

<[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015)

²⁵ Above, n.7 at para 19, p316-317

prohibiting bribery and consignment sales.²⁶ The FAAA prohibits a brewer or a wholesaler from requiring a retailer, by way of agreement or otherwise, to purchase those products to the exclusion, in whole or in part, of similar products sold by others.²⁷ The Act also prohibits retailers from entering tied house agreements with suppliers or wholesalers.²⁸ This is achieved by provisions that prevent the brewer²⁹ or wholesaler from inducing a retailer to purchase from him on a basis that would result in the exclusion in whole or in part of similar products.³⁰ The unlawful inducements include ‘acquiring an interest in property used by the retailer in his business; guaranteeing a loan of the retailer; providing excess credit; or requiring quota sales.’³¹ Consequently, Federal law does not specifically require a mandatory wholesaler tier in the distribution of alcohol as it only outlaws certain practices between brewers and retailers.³² Ronnenberg highlights that the intention was to prevent measures that had been labeled in various studies as pre-prohibition abuses.³³

Cooper and Wright subsequently note the existence of a “*complex web of regulations*” controlling the distribution and sale of alcohol in different States.³⁴ However, almost every State instituted a form of the 3-tier system under which the beer tie was effectively outlawed as an illegitimate business model and the use of wholesalers became obligatory.

²⁶ Above, n.10 at p2206. See also The FAAA Title 27, Chapter 8, Subchapter I s.205 on unfair competition and unlawful practices. (‘United States Code’ (*Office of the Law Revision Counsel*) <[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015)

²⁷ FAAA Title 27, Chapter 8, Subchapter I s.205 on unfair competition and unlawful practices. (‘United States Code’ (*Office of the Law Revision Counsel*) <[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015). See also above, n.7 at para 20, p317.

²⁸ FAAA Title 27, Chapter 8, Subchapter I s.205(b) on unfair competition and unlawful practices. (‘United States Code’ (*Office of the Law Revision Counsel*) <[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015)

²⁹ The FAAA applies to all producers of alcoholic beverages

³⁰ FAAA Title 27, Chapter 8, subchapter I s.205 on unfair competition and unlawful practices. (‘United States Code’ (*Office of the Law Revision Counsel*) <[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015) See also H.W. Ronnenberg, ‘The American brewing industry since 1920’ in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p199

³¹ FAAA Title 27, Chapter 8, Subchapter I s.205 on unfair competition and unlawful practices. (‘United States Code’ (*Office of the Law Revision Counsel*) <[http://uscode.house.gov/view.xhtml?req=\(title:27%20section:205%20edition:prelim\)%20OR%20\(granuleid:USC-prelim-title27-section205\)&f=treesort&edition=prelim&num=0&jumpTo=true](http://uscode.house.gov/view.xhtml?req=(title:27%20section:205%20edition:prelim)%20OR%20(granuleid:USC-prelim-title27-section205)&f=treesort&edition=prelim&num=0&jumpTo=true)> accessed 4th July 2015) Section 205(b) lists 7 unlawful inducements

³² Above, n.10 at p2206

³³ H.W. Ronnenberg, ‘The American brewing industry since 1920’ in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p199

³⁴ J.C. Cooper and J.D. Wright, ‘Alcohol, antitrust, and the 21st Amendment: An Empirical Examination of Post and Hold Laws’, (2012) 32 Int’l Rev.L & Econ. 379 at 379

By prohibiting economic relationships between producers, wholesalers and retailers, the system essentially requires brewers to sell to wholesalers who can only sell on to retailers or other wholesalers.³⁵ Brewers in most States therefore can no longer wholesale their own beer and are precluded from owning or having an interest in businesses that retail beer although some States permit brewers to own distribution facilities.³⁶ Some States require that beer be sold at the same price to all wholesalers, whilst others permit a degree of price competition.³⁷ The manufacturers, distributors and retailers all require a separate licence from the State, and licensees in one tier cannot be licensed to operate in another tier.³⁸ Consequently the overriding effect has been that beer producers can no longer directly supply any retail outlets, placing distributors at the centre of the US system of distribution and preventing the re-emergence of the much-feared tied houses.³⁹ Therefore, whilst burdensome, Robertson highlights that the scheme is justified on the basis that it avoids the “*perceived social ill of brewers operating their own bars or saloons*”, which was one of the main drivers behind Prohibition.⁴⁰ However, under this structure where beer sales pass through distributors as ‘middle men’, Reeves makes it clear that “*efficiency is not, to put it mildly, an achievable goal under such a regime.*”⁴¹

2.1.2 The shaping of the modern US market

The US market changed dramatically following Prohibition and the introduction of the 3-tier system. Today, following decades of consolidation it is no longer a fragmented and locally orientated business but is a classic duopoly.⁴² This process of consolidation began after Prohibition. Having been largely redundant for fourteen years, brewers faced new challenges beyond the 3-tier system. These included the soft drinks industry, which as noted by Mittelman, had grown during Prohibition and subsequently became a post-

³⁵ Above, n.10 at p2201

³⁶ Above, n.7 at para 23, p318.

³⁷ Ibid at para 31, p319. Cooper and Wright note that some states have implemented ‘post and hold’ laws. These require alcohol distributors to share their future prices by ‘posting’ them in advance and ‘holding’ them, allowing rivals to reduce their prices in line with those disclosed. These have, however, been subject to numerous challenges on the basis of facilitating wholesaler collusion. See above, n.34 at 379.

³⁸ A.M. Reeves, ‘Protecting our barefoots: Policy problems in the international wine market’ (2010) 27 Ariz. J. Int’l & Comp. L. 835 at 866-867. Some states created monopolies to handle alcohol sales, with wholesalers and distribution facilities being state owned; whilst others created agencies to issue licences to private companies to deal in the production, distribution and sale of alcoholic beverages. See also C Robertson, *The Little Book of Wine Law* (Chicago, American Bar Association, 2008) at p116-117

³⁹ Under this system, distributors in the US depend on the brewers pricing their products so as to enable the distributor to earn a profitable margin. Above, n.5 at p45

⁴⁰ C Robertson, *The Little Book of Wine Law* (Chicago, American Bar Association, 2008) at p117. See also A.M. Reeves, ‘Protecting our barefoots: Policy problems in the international wine market’ (2010) 27 Ariz. J. Int’l & Comp. L. 835 at 867

⁴¹ A.M. Reeves, ‘Protecting our barefoots: Policy problems in the international wine market’, (2010) 27 Ariz. J. Int’l & Comp. L. 835 at 867

⁴² Above, n.1 at p254. See also n.5, at p3

Prohibition source of competition for brewers.⁴³ Their use of modern bottling equipment encouraged brewers to develop new packaging options, with brewers beginning to produce canned beer by 1935.⁴⁴ Old problems of wide scale advertising and marketing also persisted and posed problems for brewers used to doing business on a local basis, selling at the point of consumption.⁴⁵ Mittelman notes that with repeal of Prohibition, familiar issues of competition between local, regional and national brewers resurrected themselves and the trend towards consolidation intensified.⁴⁶ This was further encouraged by the fact that, in contrast to the UK's preference for draft beer consumed in public houses, the US was witnessing a noticeable move away from draught to canned beer.⁴⁷ Subsequently there was also a move away from on-licensed to home consumption of beer, with the economies of scale in canning being such that only the largest brewers could take advantage of these economies. As a result, national mass marketed brands became noticeable in the 1950-1960s.⁴⁸

This consolidation continued during the 1970s and 1980s as small companies continued to close or were acquired by larger firms.⁴⁹ These larger producers were also able to make use of TV and national advertising to appeal to the take home market. This assisted in increasing their market share.⁵⁰ As Gourvish notes, the significant investment required to exploit economies of scale not only demanded this 'effective marketing of brands sold in large volumes' but naturally fueled the desire for horizontal and vertical integration.⁵¹ However, the 3-tier system curtailed the latter, and so, further encouraged concentration amongst brewers with the continued exit of smaller and medium sized producers as the search for scale economies continued.⁵² This contrasted with the UK beer market. There the acceptance of the beer tie as a legitimate business model appeared to permit the largest brewers to push their national brands whilst also protecting the smaller brewers by assuring them a limited but protected market for their products.⁵³ Gourvish also notes that by comparison to the UK market, the US market was more receptive to strong brand

⁴³ A Mittelman, *Brewing Battles a History of American Beer* (United States, Algora Publishing, 2008) at p106

⁴⁴ Ibid at p106

⁴⁵ Ibid at p105-106

⁴⁶ Ibid at p107

⁴⁷ Ibid at p107

⁴⁸ Above, n.5 at p3

⁴⁹ Ibid at p3

⁵⁰ Ibid at p3

⁵¹ Above, n.1 at p253

⁵² Ibid at p254

⁵³ Ibid at p259-260. See also Chapter 2.

advertising and canned products.⁵⁴ This further aided the growth of a small number of leading brands, with this concentration continuing for several years.⁵⁵

2.2 The US beer market today

Two of the most significant changes in the US beer market occurred in 2008 and concluded many years of consolidation. This also caused the US market to be transformed into a duopoly.⁵⁶ First, London based SABMiller entered into a joint venture with Molson Coors to form MillerCoors. Secondly, in November of that year Anheuser Busch (AB), the largest brewer in America was acquired by Belgian based InBev to form AB InBev thereby creating the US beer market's duopolistic market structure.⁵⁷ In 2013 AB InBev accounted for 50.4% of the US beer market share by volume followed by MillerCoors with a 29.2% market share. The market is therefore highly concentrated with the dupolists enjoying a combined market share of 79.6% whilst the top four market participants jointly hold a 90.2% market share.⁵⁸ By contrast, in the UK beer market, the top two brewers enjoyed a combined market share of 51% of the UK beer market by volume.⁵⁹ In-keeping with the globalisation of the brewing industry,⁶⁰ these four major brewers are owned by foreign multinational corporations.⁶¹ Further, given the US's longstanding outlawing of the beer tie, today the vast majority of beer sales are through the off-trade with on-trade sales only accounting for an 18.9% of the US beer market distribution by value in 2013.⁶² By contrast, supermarkets were the leading distribution channel accounting for 61.1% of the market's total value.⁶³ Whilst there has been a shift in favour of off-trade sales in the UK in recent years, in the UK beer market in 2013 supermarkets accounted for 35.3% of the market's value while the on-trade accounted for 42.8%.⁶⁴

2.2.1 Craft beer boom – relaxation in 3-tier distribution system

Over a relatively short history, and aided by the 3-tier system, the American industry has therefore been transformed from a fragmented and locally orientated business pre-

⁵⁴ Above, n.1 at p260

⁵⁵ Above, n.7 at para 28, p318-319

⁵⁶ Above, n.5 at p v

⁵⁷ Ibid at p3

⁵⁸ Heineken held a 6% share of the US beer market by volume in 2013 followed by Grupo Modelo S.A.B. de C.V. with 4.6%. Others accounted for 9.8%. See MarketLine, 'MarketLine Industry Profile Beer in the United States' (August 2014) at p12

⁵⁹ MarketLine, 'MarketLine Industry Profile Beer in the United Kingdom' (August 2014) at p12

⁶⁰ The increasing participation of international brewers in the UK market was also discussed in Chapter 2.

⁶¹ These are AB Inbev, based in Belgium; British based SABMillerCoors; Modela, which is now Belgian owned; and Heineken, which is based in the Netherlands. See n.5, at p3.

⁶² Above, n.58 at p13

⁶³ Ibid at p13

⁶⁴ Above, n.59 at p13

Prohibition into one that is concentrated and national in character and more recently a duopoly.⁶⁵ Now the US market is largely stagnant and mature overall and is essentially made up of three segments. These are craft beer, non-craft ‘traditional’ beer and import beer.⁶⁶ One consequence of the 3-tier system and a duopolistic market structure has been a restriction on consumer choice with the duopolists’ products dominating the market. Recently however there have been positive movements towards greater diversity. This has been the result of the recent boom in the craft beer sector. Adams notes that in this sector products are sold locally or regionally and are differentiated by the raw materials used; not TV advertising as favoured by the largest brewers.⁶⁷ The growth in this sector however has been facilitated by a relaxation in the long established prohibition of the beer tie. This has followed significant demand amongst American consumers for greater localism and choice in brewing products.⁶⁸ Welch suggests that over the past twenty years the American palate has bored of the products produced by the largest brewers, such as Budweiser and Miller.⁶⁹ As a result, in 1993 ‘brewpubs’ became legal in virtually all States through amendments to state laws prompted by these changes in consumer preferences.⁷⁰ By 2011 only a few States continued to outlaw them.⁷¹

Welch highlights that ‘brewpubs’ differ from all other brewery categories as they produce their own product and also serve it on their own premises.⁷² This clearly contravenes the 3-tier system under which they have generally been prohibited by State laws known as ‘tied house statutes’. As mentioned above these prohibit ownership of licenses in more than one tier of manufacturing, retailing or distributing alcohol⁷³ and have their roots in the general ‘distrust of domination of the industry by a few companies’.⁷⁴ Brewpubs have been legalised not through the abolition of these statutes but by creating a narrow exception to

⁶⁵ Above, n.5 at p6

⁶⁶ Ibid at p6

⁶⁷ W.J. Adams, ‘Beer Markets in Germany and the United States’ (2006) 20(1) Journal of Economic Perspectives 189 at p201

⁶⁸ Above, n.43 at p190-191

⁶⁹ J.M. Welch, ‘The Inevitability of the brewpub: legal avenues for expanding distribution capabilities’ (1997) 16 Rev. Litig. 173 at 174

⁷⁰ Prior to 1984 brewpubs were illegal in virtually all states but by 1993 they were legal in all but eight states. (Stanford University Graduate School of Business ‘Note on the US Craft Brewing Industry’ (*Stanford University Graduate School of Business*, September 1994) <<http://www.gsb.stanford.edu/faculty-research/case-studies/note-us-craft-brewing-industry>> accessed 3rd March 2015)

⁷¹ By 2000 there were 1,400 small scale beer producers in operation in the US. See D Persyn, J.F.M. Swinnen and S Vanormelingen, ‘Belgian beers: where history meets globalization’ in J.F.M. Swinnen ed, *The Economics of Beer* (New York, Oxford University Press Inc., 2011) at p94. At this time, the top 4 US producers (Anheuser Busch, Miller, Coors and Pabst) accounted for 95% of the US market (see above, n.67 at Table 1, p190). By 2003, craft production only accounted for 3.2% of domestic output (above, n.67 at p201). However, the total volume of craft beer produced continues to increase (above, n.5 at p7)

⁷² Above, n.69 at p175

⁷³ Ibid at p175-176

⁷⁴ Ibid at p179

these rules.⁷⁵ Strict requirements are imposed on ‘brewpubs’, including production limits and restrictions on where and to whom their products can be sold.⁷⁶ Welch notes that owners of ‘brewpubs’ can be prohibited from having interests in other ‘brewpubs’.⁷⁷ They are also often precluded from selling to grocery stores, bars and restaurants and even distributors, thereby preventing any off sales, much to the frustration of these smaller brewers.⁷⁸

In 2011 craft beer only accounted for 5.7% of the total US beer market by volume and in April 2012 there were 2000 craft brewers in operation in the US.⁷⁹ However, such is the popularity of craft beer that many of the traditional national brewers, who for so long have been shielded from competition from such craft brewers by virtue of the tied house statutes, have been forced to acquire some of this market via internal growth and acquisitions.⁸⁰ This suggests that US consumers are no longer satisfied with the offer of only generic mass-produced beers of the largest brewers which since the introduction of the 3-tier system have come to dominate the market. Limited acceptance of the beer tie through strict exceptions to the tied house statutes, which for decades have deemed the beer tie an illegitimate business model in the US, has been central in increasing diversity. Such diversity has long been a feature of the UK beer market due to, amongst others, toleration of the beer tie. This is so even although this diversity is not necessarily reflected in the pubco dominated on-trade sector as discussed in Chapter 4. Acceptance of the beer tie as a legitimate business model has ultimately helped smaller brewers in the UK to survive by retaining their small but protected market shares in the face of challenge from the UK’s largest brewers. Whilst as discussed in Chapter 2 concerns have long been expressed over the national, and now international, brewers’ domination of the UK beer market, Welch correctly highlights that the concerns in the US over monopolisation within the brewing industry which prompted a very strict approach to tied houses, and is the antithesis of the UK market, have done little to prevent a similar domination of the US beer industry by the largest brewers.⁸¹

⁷⁵ Ibid at p176

⁷⁶ Ibid at p176

⁷⁷ Ibid at p176

⁷⁸ Ibid at p176

⁷⁹ Above, n.5 at p7

⁸⁰ Ibid at p8

⁸¹ Above, n.69 at 180

2.2.2 Brewer control of US wholesalers

In contrast to the UK beer market however under the 3-tier system wholesalers have a central role in the US market. This differs from the UK where, as discussed in Chapter 4, an independent wholesale and distribution sector has failed to materialise with this being a source of concern in successive UK competition law investigations. As noted above, the 3-tier system was implemented to ensure legal separation between brewers, distributors and retailers with wholesalers being of significant importance in achieving this. The intention was to limit the ability of one tier within the system to control another,⁸² as is evident in the UK beer market today through pubco ownership of public houses. There are no pubcos operating in the US market. In order to prevent any overlap between the tiers in the US market the role of the wholesaler has been further ensconced by the enactment of franchise protection laws in many States. These make it extremely difficult for suppliers to end their contractual relationship with wholesalers, as well as requiring brewers to grant wholesalers exclusive territories.⁸³ As Cooper notes, such franchise laws often prohibit the termination of wholesalers contracts in the absence of “*just cause*” with extensive administrative processes to be satisfied before this requirement is deemed to have been met.⁸⁴ As Tamayo and Cooper highlight the underlying intention was to create a more level playing field between the parties, as wholesalers were generally considered to be small and suppliers generally large.⁸⁵ These franchise protection laws were also to protect the welfare of citizens by ensuring ‘orderly and fair’ distribution of alcohol within the State.⁸⁶ However, despite these protections, distributors are generally considered to be in a vulnerable position within the US market. Their survival is directly linked to the existence of the 3-tier system and they are also susceptible to consolidation and cost savings by brewers and retailers.⁸⁷

2.2.3 Wholesaler consolidation

Despite the highly protected position of wholesalers in the US market, the wholesale sector has consolidated with there now being many producers and few wholesalers operating in

⁸² D.S. Sibley and P Srinagesh ‘Dispelling the Myths of the Three-tier distribution system’ at p6 (*Five Star Wine and Spirits*, Fall 2008) <http://www.five-star-wine-and-spirits.com/includes/archivos/about_five_star/pdf/three_tier_01.pdf> accessed 4th March 2015

⁸³ Above, n.34 at footnote 1, p379. See also above, n.5 at p45-46

⁸⁴ Above, n.34 at footnote 1, p379

⁸⁵ Above, n.10 at p2214 and n.34 at footnote 1, p379

⁸⁶ Above, n.34 at footnote 1, p379

⁸⁷ Above, n.5 at p46

the US beer market.⁸⁸ These remaining wholesalers however continue to enjoy a protected position and also wield significant power under the 3-tier system.⁸⁹ This increased consolidation within the wholesale sector has brought the US market more into line with the UK beer market, which as already mentioned above lacks a competitive wholesale sector. This has increased the difficulties faced by start-up brewers wishing to have their products distributed. These smaller brewers have significant difficulty persuading powerful wholesalers to carry their products as they are not as profitable as those produced by the largest brewers.⁹⁰ Consequently, smaller brewers are often forced to find alternative means of getting their product to market, which are not always the most efficient.⁹¹

Furthermore, once accepted by a distributor smaller producers can continue to face difficulties in having their products distributed. By using value-added distributors to handle the merchandising, sale and delivery of their products, brewers generally benefit from high returns and low capital requirements under the 3-tier system. This contrasts with distributors who often suffer lower returns and higher capital requirements as they have to fund distribution networks.⁹² Distributors are therefore incentivised to actively encourage the sale of those brands with the highest profit margins, which are usually those produced by the largest brewers.⁹³ This has also caused further consolidation within the distribution sector in order to reduce costs and so offset margin pressure.⁹⁴

The remaining powerful wholesalers in the US beer market are also influential in State politics.⁹⁵ Welch highlights that in some States, such as Texas, wholesalers opposed deregulation of the 3-tier system and ‘brewpub’ legislation.⁹⁶ This has been attributed to their fear of being bypassed should producers be able to sell directly to consumers.⁹⁷ Tamayo therefore highlights that in the US market, craft brewers face tough opposition from

⁸⁸ In the period 1980-2010, the number of distributors in the US declined from approximately 5,000 to just over 2,000. The American Antitrust Institute notes that this is widely used industry data that may not be fully accurate. See above, n.5 at p9.

⁸⁹ Above, n.12 at p6. See also above, n.5 at p46.

⁹⁰ Above, n.41 at p867

⁹¹ Some have gone to the extreme of creating their own distribution and wholesale companies. Reeves provides the example of Stone Brewery California. See above, n.41 at p867.

⁹² Deloitte, ‘Profitable growth and value in the beer industry A view from Deloitte and SAP’ at p3 (*Deloitte*) <https://www.deloitte.com/assets/Dcom-Venezuela/Local_Assets/Documents/White_Paper_Beer%281%29%282%29.pdf> accessed 2nd March 2015

⁹³ Ibid at p3

⁹⁴ Ibid at p3

⁹⁵ The National Beer Wholesalers Association is in the top 30 donors to Federal candidates. Above, n.12 at p6. See also n.5 at p46

⁹⁶ Above, n.69 at p182

⁹⁷ Ibid at p182

wholesalers whose well-resourced and powerful lobbyists have protected their economic interests under the 3-tier system by successfully opposing deregulation in some States.⁹⁸

2.2.4 Wholesaler exclusivity

The number of distributors and wholesalers operating in the US market has therefore declined with many medium sized multi-brand wholesalers being bought out by larger wholesalers while smaller operators have left the market.⁹⁹ Further, the majority of those remaining often exclusively handle certain brands and identify themselves with the major brewers.¹⁰⁰ Distributors of Coors, AB and Miller products are estimated to account for 60% of the number of distributors in the US market and for 89% of the volume of beer distributed.¹⁰¹ This situation contributes to the difficulties independent producers experience in getting their products to the market. Further parallels with the UK beer market where the largest brewers still largely control the distribution of beer were evident in the US market throughout the 1990s. AB introduced its “*100 per cent share of mind*” marketing philosophy, which actively encouraged distributors to carry only their products and caused other brewers’ products to be dropped by their distributors.¹⁰² This practice was not exclusive to AB with other brewers offering financial incentives in exchange for loyalty and exclusivity.¹⁰³

Despite these difficulties, more recently due to the increasing demand for craft beer there has been a shift in this long-established trend of wholesalers favouring larger brewers’ products. Distributors in the US have started to move towards multiple clients, including craft brewers.¹⁰⁴ Some distributors have also emerged that handle only craft beer and craft brewers themselves have taken steps to establish their own distribution networks.¹⁰⁵ However, whilst these are undoubtedly positive market developments, in 2012 it was estimated that AB owned in excess of twelve distributors and has minority shareholdings in others.¹⁰⁶ It also has contracts with approximately 500 distributors.¹⁰⁷ The majority of these distributors handle AB products exclusively although there has been some relaxation

⁹⁸ Above, n.10 at p2230

⁹⁹ Above, n.5 at p10

¹⁰⁰ Ibid at p10

¹⁰¹ Ibid at p9-10

¹⁰² Above, n.69 at p181-182

¹⁰³ Above, n.10 at p2217

¹⁰⁴ Above, n.5 at p10

¹⁰⁵ Above, n.10 at p2217. See also above, n.5 at p10.

¹⁰⁶ Above, n.5 at p9-10. It was estimated that approximately 2000 distributors were operating in the US in 2010, although there are doubts over the accuracy of this data (ibid at p10).

¹⁰⁷ Ibid at p9

to allow them to handle other brewers' products including craft brewers.¹⁰⁸ There are also similar arrangements in place for the distribution of major brands Miller and Coors.¹⁰⁹ In light of these on-going difficulties experienced by US craft brewers in getting their products to market there are some similarities with the position of small brewers in the UK who, as discussed in Chapter 4,¹¹⁰ have struggled to comply with the significant demands of pubcos in order to have their products distributed.

2.2.5 Constitutional protection for the 3-tier system but some exceptions being created

By virtue of its constitutional protection under the 21st Amendment discussed above, the 3-tier system has generally been shielded from any great erosion. This has only recently begun to change with some minor exceptions being created to facilitate 'brewpubs' discussed above and more recently Washington's Initiative 1183.¹¹¹ In 2011 Washington State opted to end its monopoly on liquor sales (sales of beer, wine and spirits) by selling its alcohol distribution centres and liquor stores to private companies.¹¹² The State now issues licences to private companies to carry out these activities.¹¹³ Initiative 1183 eroded the 3-tier system in Washington as retailers are now able to purchase directly from producers, have freedom to negotiate discounts and can store their inventories in their own warehouses.¹¹⁴ The Initiative was prompted as it would allow the competitive private sale of liquor under State regulation. This would free State officials from dealing with retail sales and allowing them to focus on the enforcement of the State's liquor and public health laws.¹¹⁵ The Initiative's sponsors noted, amongst others, that the regulations imposing the Government's monopoly on both wholesale and retail liquor sales were outdated and inefficient and so costly to all parties.¹¹⁶ It was suggested that the privatisation of liquor sales in the State would increase revenues through the imposition of a fee on privately owned liquor retailers and wholesalers operating in the State. However notwithstanding the

¹⁰⁸ Ibid at p10

¹⁰⁹ Ibid at p10

¹¹⁰ Chapter 4, p119

¹¹¹ Craft brewers and wineries have challenged the three-tier system through court actions. Above, n.5 at p44-45

¹¹² J Mercier, 'Citizens' Guide to Initiative 1183: To End Washington's Liquor Store Monopoly' (*Washington Policy Centre*, September 2011) <<http://www.washingtonpolicy.org/publications/notes/citizens-guide-initiative-1183-end-washingtons-liquor-store-monopoly>> accessed 5th March 2015

¹¹³ Washington State Liquor Control Board, 'I-1183 Transition' (*Washington State Liquor Control Board*) <<http://liq.wa.gov/transition/overview>> accessed 5th March 2015). As of 1st June 2012, the Washington State Liquor Control Board ceased state liquor store and liquor distribution operations. State-run liquor stores closed and state distribution assets were sold. This was replaced by private distribution and liquor sales by those granted licences to do so by the State. See above, n.5 at p44.

¹¹⁴ Above, n.112 and above, n.5 at p44-45

¹¹⁵ Above, n.112

¹¹⁶ Ibid quoting the 'Intent' section for I-1183

touted benefits of the Initiative, concerns were also expressed that it may present an opportunity for large retailers, such as Costco, to dominate liquor sales and distribution. Costco Wholesale had reportedly allocated \$22 million to push through the Initiative.¹¹⁷ Nevertheless, other States including Virginia, Oregon and Pennsylvania are considering such measures, with more likely to follow suit in bringing about such privatisation due to increasing pressure on State Governments to cut costs and increase revenues.¹¹⁸

2.3 '3-tier' distribution is not a fix-all solution for the distribution of beer

In light of the foregoing, it would appear that merely outlawing the beer tie as an illegitimate business model and imposing a mandatory separation between each tier in the chain of distribution does not produce a very competitive system for the distribution of beer, and as such does not provide a suitable model for the UK market to follow. There are however lessons to be learned from the experience of the US market following the outlawing of the tie which can inform the proposals made in the thesis for the reform of the UK market. As noted above, since the implementation of the 3-tier system of manufacturing, wholesaling and distributing liquor following Prohibition, the US beer market has experienced significant concentration, with a resulting impact on consumer choice in the market. The US beer market has changed from a largely local and fragmented market pre-Prohibition to a modern day duopoly under the 3-tier system with supermarkets now dominating the distribution channel for beer. The 3-tier system has therefore failed to shield the US market against the dangers of monopolisation by a few large brewers, which was considered to be the primary danger of vertical integration and was one of the main drivers behind the implementation of the 3-tier system. Consolidation is however a recognised feature of the global beer market and as discussed in Chapter 2, has also affected the UK beer market. Numerous factors have contributed to this including technological advances, declining consumption, and the desire for scale economies. However, the restriction on vertical integration by outlawing the beer tie as a legitimate business model after Prohibition has been shown to have been one of the initial catalysts for this concentration in the US market. Consequently it is necessary to be aware of this when proposing reforms to the UK beer market.

Furthermore, whilst the craft beer sector of the US market has recently enjoyed a gain in market share, this has been facilitated almost entirely by a relaxation in the 3-tier system

¹¹⁷ M Allison, 'Taking a clear look at liquor initiative I-1183' (*The Seattle Times*, 22nd October 2011) <http://seattletimes.com/html/business/technology/2016583207_liquor23.html> accessed 5th March 2015. See also above, n.112.

¹¹⁸ Above, n.5 at p44-45

through some acceptance of vertical integration. This is exemplified by the ‘brewpub’ exceptions now implemented in most States. As discussed in Chapter 2, smaller brewers operating in the UK beer market have long enjoyed the advantages of being able to sell their products from their premises, or those tied to them, thereby affording them a small but protected market share in face of competition from major brewers.¹¹⁹ Following the implementation of the ‘brewpub’ exceptions small brewers in the US are only just coming to benefit from this. This relaxation in the 3-tier system has therefore also brought about as increase in consumer choice in the US beer market by facilitating the sale of beers beyond those of the duopolists and other large brewers. By contrast, the UK beer market has long enjoyed the increased consumer choice offered by its established craft beer sector, even if this is not reflected in the pubco dominated on-trade.¹²⁰ It is therefore necessary that any reforms of the UK market acknowledge this role of the tie in protecting the market position of small brewers.

However, as discussed above, the UK beer market has long lacked an independent wholesale and distribution sector with this being a long-standing concern in successive investigations by the UK competition authorities. By contrast wholesalers have played a central role in the distribution of beer in the US market. In recognition of their importance they enjoy both Federal and State protection. Nevertheless, in light of the numerous issues surrounding their practices in the US market including their alignment with the duopolists, the imposition of a mandatory 3-tier system does not guarantee the creation and operation of an ‘independent’ wholesale and distribution sector. Additional measures would be required to ensure their independence beyond those in place under the US regulatory regime, such as a prohibition on wholesalers acting exclusively for a single brewer. Therefore, whilst as noted in Chapter 2 there are numerous problems associated with the operation of the beer tie in the UK, a mandatory 3-tier system poses different challenges some of which serve to highlight the benefits of vertical integration through some acceptance of the beer tie as a legitimate business model. Consequently, regard will now be had to the distribution of beer in Australia where the tie has more recently been outlawed but a mandatory 3-tier system of distribution has not been imposed.

¹¹⁹ Regional preferences for real ale and a variety of beers also helped with this. See T.R. Gourvish, ‘Concentration, diversity and firm strategy in European brewing, 1945-1990’ in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p90

¹²⁰ As discussed in Chapter 4, there have been concerns over pubcos limiting consumer choice by restricting the beers that can be sold through their tied and managed estates.

3. The Australian beer market

Similarly to the US, Australia is a major beer producer. It has also been forced to deal with brewers' extensive use of beer tying agreements however in doing so has adopted a different approach from that in the US. As noted above, in the US social concerns influenced the Prohibition movement in the early twentieth century and prompted the beer tie to be regarded as an illegitimate business model in all circumstances, with some minor exceptions only recently being accepted. In Australia, brewers' reliance on the beer tie has been affected by Australian competition law provisions that outlaw exclusive dealing where this is likely to result in a substantial lessening of competition.

3.1 A brief overview of the historical development of the Australian beer market and brewers' reliance on the beer tie

Similarly to the UK and the USA, Australia has a long history of brewing with it being one of the earliest manufacturing activities of the colonies.¹²¹ Today, Australians are amongst the largest per capita consumers of beer in the world. However during the 19th century, due to poor transportation and the perishable nature of beer, the brewing industry was dispersed with many small-scale brewers operating in towns as part of local hotels rather than as individual specialist brewers.¹²² By the end of the century a more modern industry focused on large-scale and capital-intensive production methods had evolved following advances in brewing methods suited to hot climates.¹²³ The introduction of lager beer in 1880 also came to be popular with consumers.¹²⁴ As this expansion continued, State laws were passed to regulate the sale of alcohol.¹²⁵ Similarly to the UK this was based on a licensing system for those wishing to sell liquor. The principle outlets were hotels selling beer in bottled and draught form and brewers made it a priority to tie up these hotels and other

¹²¹ G Oliver, ed, *The Oxford Companion to Beer* (New York, Oxford University Press Inc., 2012) at p70-71. See also D.T. Merrett, 'Stability and change in the Australian brewing industry, 1920-1994' in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p230. For discussion on beer brewing in the colonies see D Hughes, 'The brewing industry in early Australia' in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p214-215.

¹²² D.T. Merrett, 'Stability and change in the Australian brewing industry, 1920-1994' in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p230 and G Oliver, ed, *The Oxford Companion to Beer* (New York, Oxford University Press Inc., 2012) at p71

¹²³ D.T. Merrett, 'Stability and change in the Australian brewing industry, 1920-1994' in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p230. See also G Oliver, ed, *The Oxford Companion to Beer* (New York, Oxford University Press Inc., 2012) at p71.

¹²⁴ G Oliver, ed, *The Oxford Companion to Beer* (New York, Oxford University Press Inc., 2012) at p71

¹²⁵ D.T. Merrett, 'Stability and change in the Australian brewing industry, 1920-1994' in R.G. Wilson and T.R. Gourvish, eds, *The Dynamics of the International Brewing Industry since 1800* (Oxfordshire, Routledge, 1998) at p231

distribution channels.¹²⁶ Dunstan notes that brewers claimed it was necessary to control the hotels serving their products in order to ensure, amongst others that they were properly run and their beer was not watered down.¹²⁷ However, as the temperance movement strengthened and the number of licences being issued slowed, the barriers to entry into the industry increased, with Merrett noting that by the 20th Century the tie was a form of forward integration widely utilised by brewers.¹²⁸ By 1870 -1880 half of the hotels in Victoria and metropolitan New South Wales (NSW) were already tied to a brewer.¹²⁹ In line with their British peers, the Australian brewers sought to form close relationships with those outlets that agreed to exclusively serve their products.¹³⁰ By the 1920s the vast majority of country brewers had been ousted by the city brewers who had replaced them with branch plants, with Merrett noting that the industry now represented its 'modern form'.¹³¹ As a result, the industry fell into the clutches of a small number of large-scale capital-intensive brewers. However Oliver notes that given Australia's largely dispersed population each of the major brewers were independent and were based in a capital city or significant town in each State and consumers were loyal to their local beer brands.¹³²

These brewers were able to deny competitors a market share by entering into tying agreements with large numbers of hotels that were limited to serving only their products.¹³³ Kirby notes that this tied house system strengthened during the Depression of the 1930s and World War II.¹³⁴ Eventually in 1951, amidst concerns regarding corruption in pubs, the NSW Government appointed a Royal Commission to review brewery ownership of tied houses.¹³⁵ The terms of reference for the Commission were, amongst others, to examine brewers' financial interests in and control of hotels, and the adequacy of the liquor licensing laws in controlling licensing.¹³⁶ It established that 69% of the hotels in the area were tied to the two major brewers.¹³⁷ While the Committee failed to find any specific disadvantages associated with the operation of the tied house system, the report on the

¹²⁶ In Australia, pre-1950, with the exception of clubs, only hotels were licensed to sell beer on draught. Above, n.125 at p231 and p238. See also K Dunstan, *The Amber Nectar A celebration of beer and brewing in Australia* (Victoria, Viking O'Neil, 1987) at p35

¹²⁷ K Dunstan, *The Amber Nectar A celebration of beer and brewing in Australia* (Victoria, Viking O'Neil, 1987) at p148

¹²⁸ Above, n.125 at p232

¹²⁹ Ibid at p232

¹³⁰ Ibid at p232

¹³¹ Ibid at p232

¹³² Above, n.124 at p71-72

¹³³ Above, n.125 at p235

¹³⁴ D Kirkby et al, *The Australian Pub* (Sydney, UNSW Press, 2010) p100

¹³⁵ Ibid at p100

¹³⁶ Royal Commission on Liquor Laws in New South Wales, *Final Report of Commission* (New South Wales Government State Records, 25th March 1954)

<<http://investigator.records.nsw.gov.au/Entity.aspx?Path=%5CAgency%5C4925>> accessed 5th March 2015

¹³⁷ Above, n.134 at p105

conduct of hotels was damming.¹³⁸ It was not, however, considered to be in the public interest or financially practical to abolish the tied house system.¹³⁹ Instead it was considered acceptable for brewers to own hotels provided they appointed managers and were not themselves directly involved in the running of those establishments.¹⁴⁰ By the early 1970s the South Australian Brewing Company controlled more than 50% of hotels in the State of Victoria while brewers Tooths and Tooheys had in some manner tied approximately 70% of the hotels in NSW by the early 1950s.¹⁴¹ The tied house system in Australia therefore served as a substantial barrier to new entrants to the market and perpetuated the significant level of concentration within the industry.¹⁴²

More generally across the country however, given the significant market power enjoyed, and in the absence of any legislation constraining concentration or anti-competitive practices, Merrett notes that brewers came to their own implicit understandings regarding the level and the type of competition between them.¹⁴³ Where two or more brewers operated in the same market, price competition was absent and brewers would engage in price wars with any brewer who did not respect these arrangements.¹⁴⁴ Stubbs highlights that as early as 1901, brewers Tooths and Tooheys reached agreement not to ‘interfere’ with their respective tied houses.¹⁴⁵ Instead, competition within the market was based on the acquisition of even more tied trade.¹⁴⁶

3.2 How the beer tie came to be outlawed in Australia

Having enjoyed decades without any restrictive trade practices legislation, the tide eventually turned on the Australian brewers. In the 1960s and 1970s, their stranglehold on distribution channels weakened as many anti-competitive acts were prohibited.¹⁴⁷ Included amongst these were demands by suppliers for exclusive dealing arrangements with distributors.¹⁴⁸ The route to this was not however a direct one. Whilst Australia has had a

¹³⁸ Ibid at p105

¹³⁹ Above, n.136

¹⁴⁰ Ibid

¹⁴¹ Above, n.125 at p236. See also B.J. Stubbs, ‘The revival and decline of the independent breweries in New South Wales 1946-1961’ (1996) 36(1) Aust Econ Hist Rev 32 at p35

¹⁴² B.J. Stubbs, ‘The revival and decline of the independent breweries in New South Wales 1946-1961’ (1996) 36(1) Aust Econ Hist Rev 32 at p35

¹⁴³ Above, n.125 at p236

¹⁴⁴ Ibid at p236

¹⁴⁵ Above, n.142 at p36

¹⁴⁶ Above, n.125 at p236

¹⁴⁷ Ibid at p239

¹⁴⁸ Ibid at p239

common law doctrine of restraint of trade, dating as far back as 1890,¹⁴⁹ the first national Act seeking to control anti-competitive conduct was the Australian Industries Preservation Act 1906.¹⁵⁰ This was modeled on the US Sherman Act 1890 and made it an offence to conclude a contract or combine ‘with intent to restrain trade or commerce to the detriment of the public...’.¹⁵¹ These measures did not go far enough in restraining the powerful Australian brewers. Restrictive trade practices continued largely unabated throughout the Australian industry for several decades.¹⁵² Although numerous legislative attempts to deal with the situation followed,¹⁵³ the first of any great significance was the Trade Practices Act 1974 Cth (the TPA). The then Labour Government was under pressure from the public to tackle price increases as well as inflationary pressures.¹⁵⁴ They sought to address all forms of anticompetitive behavior through penalties and injunctions under the TPA.¹⁵⁵ This subsequently instituted a stricter approach to anticompetitive behavior in light of Australia’s flagging economic predicament. It was recognised that increased competition, not protectionism, would promote economic growth and efficiency as well as consumer protection.¹⁵⁶

3.2.1 Trade practices Act (TPA) 1974

As in the UK, in Australia the general concerns regarding the extensive use of exclusive dealing arrangements, such as the beer tie, focus on their ability to aid the acquisition and exercise of market power and their potential to contribute to market foreclosure.¹⁵⁷ Clough also notes that barriers to entry are an important consideration in Australia as markets are

¹⁴⁹ This had limited application given that it was principally concerned with the preservation of the right of individuals to work and trade. The Organisation for Economic Cooperation and Development, ‘OECD Reviews of regulatory reform Competition Policy in Australia’ at p11 (*OECD*, 2010)

<<http://www.oecd.org/gov/regulatory-policy/44529918.pdf>> accessed 3rd July 2015

¹⁵⁰ Ibid at p11. See Australian Industries Preservation Act 1906

<<http://www.comlaw.gov.au/Details/C1906A00009>> accessed 5th March 2015

¹⁵¹ Section 4 Australian Industries Preservation Act 1906

<<http://www.comlaw.gov.au/Details/C1906A00009>> accessed 5th March 2015. See also above, n.149 at p11-12

¹⁵² A Fels and T Grimwade, ‘Authorisation: is it still relevant to Australian competition law?’ (2003) 11 CCLJ 187 at 188

¹⁵³ The Trade Practices Act 1965 replaced this. The only complete prohibition imposed was on collusive tendering as lobbyists had successfully watered down its provisions rendering it ineffective. Using UK legislation as a template, it introduced a system for the examination of certain restrictive agreements and practices based on a broad test of public interest, however it faced constitutional issues leading to its repeal by the Trade Practices Act 1971. See above, n.149 at p12.

¹⁵⁴ Above, n.152 at p189

¹⁵⁵ Ibid at p189

¹⁵⁶ Above, n.149 at p12

¹⁵⁷ Clough highlights the Australian Competition Tribunal’s concerns over broad generalisations that vertical restraints are pro- or anti-competitive. They consider they should be subject to an analysis that balances efficiency gains and welfare losses, similar to the approach in the EU discussed in Chapter 3. See D Clough, ‘Law and economics of vertical restraints in Australia’ (2001) 25 Melbourne University Law Review 551 at 552 and 561

relatively small and concentrated.¹⁵⁸ The UK and Australia have however adopted different approaches in addressing these concerns. As discussed in Chapter 4, the UK in line with the EU permits the beer tie to benefit from parallel exemption from the competition law provisions under Regulation 330/2010, failing which it has to meet the test set by Chapter I of the Competition Act 1998 in order for the agreement to be considered contrary to the UK competition law provisions.¹⁵⁹ This is so even although the newly adopted 2015 Act restricts the operation of the tie by requiring pub owning businesses to offer their tied tenants a Market Rent Only (MRO) option in certain circumstances.¹⁶⁰ In Australia, the TPA was a Federal Act and as such applied throughout Australia. The central antitrust provisions of the TPA were contained in s.45-s.47 and have been re-enacted as the current antitrust provisions of the Competition and Consumer Act 2010 (CCA 2010). Section 47 of the TPA outlawed the practice of exclusive dealing including the use of beer tying agreements. Under the TPA, now the CCA 2010, Australia has a dual adjudication system for assessing exclusive dealing arrangements.¹⁶¹ The Australian Competition and Consumer Commission (ACCC)¹⁶² can authorise notified conduct or grant it immunity from the statutory provisions with these authorisation decisions being subject to appeal to the Australian Competition Tribunal (Tribunal).¹⁶³

3.2.1.1 TPA – the antitrust provisions

Section 45-s.47 of the TPA contained Australia's antitrust provisions and were only concerned with the actions of corporations. While s.46 dealt with substantial market power, s.45 prohibited contracts, arrangements or understandings in restraint of trade or commerce. This was generally considered to deal with horizontal agreements between competitors. By contrast s.47 was focused on the issue of vertical agreements,¹⁶⁴ and so was of significance to brewers who placed reliance on beer tying agreements.¹⁶⁵ Section 47 prohibited the practice of 'exclusive dealing' with s.47(1) declaring that 'a corporation shall not, in trade or commerce engage in the practice of exclusive dealing.' Section 47(2)

¹⁵⁸ D Clough, 'Law and economics of vertical restraints in Australia' (2001) 25 Melbourne University Law Review 551 at 582

¹⁵⁹ See Chapter 3 and Chapter 4.

¹⁶⁰ This was discussed in Chapter 4.

¹⁶¹ Above, n.158 at p552

¹⁶² Until 1995 this was the Trade Practices Commission. For simplicity it will be referred to throughout the thesis as the ACCC.

¹⁶³ This was formerly known as the Trade Practices Tribunal. For simplicity it will be referred to throughout the thesis as the Australian Competition Tribunal (Tribunal).

¹⁶⁴ The High Court of Australia has been critical of the use of the terms of 'vertical' and 'horizontal' agreements when referring to these sections of the TPA. See N Wilson 'Anti-competitive arrangements in Australia: the devil is in the detail down under' (2011) 32(8) E.C.L.Rev 379 at 381

¹⁶⁵ Section 46 TPA dealt with substantial market power. The focus of this chapter shall be s.47 TPA given its relevance to the beer supply agreements.

then detailed a range of prohibited non-price restrictions imposed by suppliers in respect of the distribution or marketing of their goods or services by the person supplied.¹⁶⁶ Whilst s.47 is drafted in an elaborate fashion, Hurly succinctly states that exclusive dealing “*is essentially a supply of goods or services on the condition that the purchaser accept a restriction on its ability to deal.*”¹⁶⁷ Consequently s.47 was applicable to beer tie agreements under which the purchaser agrees to distribute the supplier’s goods to the exclusion of their competitors. Such agreements are also referred to in Australia as ‘solus’ contracts.¹⁶⁸ Section 47 TPA was an incredibly long and complex section due to the numerous vertical non-price restraints it was intended to deal with.¹⁶⁹ Section 47(2) stated that a corporation engages in the practice of exclusive dealing if it ‘(a) supplies, or offers to supply, goods or services; (b) supplies, or offers to supply, goods or services at a particular price; or (c) gives or allows, or offers to give or allow, a discount allowance, rebate or credit in relation to the supply or proposed supply of goods or services by the corporation’; on the condition that the person ‘(d) will not, or will not except to a limited extent, acquire goods or services of a particular kind or description, directly or indirectly from a competitor of the corporation or a related company’. Section 47(12) TPA however clarified that the prohibition on exclusive dealing under s.47 did not apply to restrictive dealings between related corporations.

However, before the exclusive dealing in question was prohibited, similarly to the EU and UK competition law provisions, s.47 TPA required consideration of the effects of the conduct on competition.¹⁷⁰ As discussed in Chapter 4, the Chapter I Prohibition of the Competition Act 1998 requires that the conduct in question affects trade within the UK or has as its object or effect the prevention restriction or distortion of competition within the UK.¹⁷¹ This appears to be a higher test than that imposed by s.47(10) TPA which simply stated that exclusive dealing was prohibited if the conduct had the ‘purpose, effect or likely effect of substantially lessening competition’.¹⁷² The majority of enforcement action under the TPA provisions has focused on notification and authorisation applications before the ACCC and the Tribunal. Hurley and McEwin therefore note that there are very few judicial

¹⁶⁶ Section 47 TPA also applied to restrictions on the supplier’s ability to deal with its goods or services. The focus here is restrictions imposed on the purchaser of goods as under a beer supply agreement. A Hurley, *Restrictive Trade Practices Commentary and Materials* (Sydney, The Law Book Company Limited, 1991) at p326-327

¹⁶⁷ A Hurley, *Restrictive Trade Practices Commentary and Materials* (Sydney, The Law Book Company Limited, 1991) at p326

¹⁶⁸ Ibid at p326

¹⁶⁹ A Bruce, *Australian Competition Law* 2nd Edition (Chatswood NSW, LexisNexis Butterworths, 2013) at para 9.10, p171

¹⁷⁰ Section 47(10) TPA

¹⁷¹ Section 2(1) Chapter 1 Competition Act 1998

¹⁷² Section 47(10) TPA. Third line forcing in s.47(6), s.47(7), s.47(8)(c) and s.47(9)(d) was prohibited *per se*.

decisions highlighting the approach of the courts in assessing the competitive impact of exclusive dealing arrangements.¹⁷³ Hurley indicates that the ACCC and Tribunal have taken a negative view where the corporations involved have enjoyed market power, the market has had high barriers to entry or where there has been a network of one-brand restriction in the market.¹⁷⁴ McEwin also highlights that ‘substantial’ means that the conduct in question must be ‘non-trivial’ in the context in which it occurs in the relevant market and through the use of ‘likely’ extends to taking into account the future impact of the conduct on competition.¹⁷⁵ Nevertheless, this still appears to be a lesser test for outlawing exclusive dealing arrangements than its equivalent under Chapter I of the Competition Act 1998.

3.2.1.2 Authorisation and notification under the TPA

As mentioned above, the majority of the enforcement action under the TPA occurred under the notification and authorisation provisions. While the intention of the TPA was to prohibit anticompetitive conduct, s.88(8) TPA made provision for the authorisation of exclusive dealing conduct with the tests for granting this being contained in s.90 TPA. These provisions opened up the possibility for the ACCC to authorise most conduct coming within the TPA.¹⁷⁶ Section 90(6) TPA contained the test for authorisation of exclusive dealing. This required that before granting any authorisation the ACCC had to be satisfied that the conduct to which the application related resulted or was likely to result in a benefit to the public, and would outweigh the detriment to the public constituted by any lessening of competition that would result.¹⁷⁷ While ‘public benefit’ was not defined in the TPA, Smith highlights that this created flexibility and permitted the application of the TPA to changing circumstances.¹⁷⁸ The TPA therefore relied on the term ‘public benefit’ as opposed to ‘public interest’ with Fels and Grimwade considering this appropriate in light of the ACCC’s need to engage in a weighing up process to determine whether or not to grant authorisation.¹⁷⁹ They note the ACCC and Tribunal’s practice of applying a ‘future with-and-without test’ to determine the net public benefit through consideration of the

¹⁷³ Above, n.167 at p327. See also R.I. McEwin, ‘Vertical Restraints in the Australian Trade Practices Act’ (1994) 9 Rev Ind Organ 627 at 629

¹⁷⁴ Above, n.167 at p327. See also above, n.158 at 593

¹⁷⁵ R.I. McEwin, ‘Vertical Restraints in the Australian Trade Practices Act’ (1994) 9 Rev Ind Organ 627 at 230

¹⁷⁶ Above, n.152 at footnote 14, p190

¹⁷⁷ Section 90(6) TPA

¹⁷⁸ R Smith, ‘Authorisation and the Trade Practices Act: More about public benefit’ (2003) 11(1) C.C.L.J. 1 at p2

¹⁷⁹ Above, n.152 at p200

situation with and without the conduct in question.¹⁸⁰ They also highlight that the basis for granting an authorisation was “*the presumption that the conduct creates sufficient public benefit that it is desirable, on balance, even though it may also give rise to some anti-competitive effects.*”¹⁸¹

Consequently, this authorisation process was not entirely dissimilar to the European Commission’s initially exclusive ability to grant exemptions under Article 101(3) Treaty on the Functioning of the European Union (TFEU) to agreements infringing Article 101(1) discussed in Chapter 3.¹⁸² However, the requirements of Article 101(3) TFEU are more focused on efficiency considerations than the public benefit condition of s.90 TPA. As Clough notes the small and concentrated nature of Australia’s markets have influenced what is taken into consideration in determining what is relevant to the public benefit.¹⁸³ As such, he states that efficiency considerations have not been the primary concern for the ACCC although he suggests that there has been increasing recognition of efficiency as a public benefit.¹⁸⁴ Hanks and Williams also highlight the lack of consideration the ACCC has given to efficiency considerations as creating public benefits.¹⁸⁵ These observations are in line with Fels and Grimwade’s assertion that “[a]uthorisation reflects the belief that the public interest, with an emphasis on an efficient and productive economy, is the centerpiece of the TPA and that competition is not an end in itself.”¹⁸⁶

In recognition of the potential benefits of exclusive dealing however s.93 TPA also made special provision for the notification of exclusive dealing arrangements, thereby distinguishing them from all other conduct falling within the terms of the TPA.¹⁸⁷ This opened up the possibility for the conduct in question to be granted a statutory interim exemption from the TPA. This exemption could be withdrawn by the ACCC issuing a notice confirming that the notified conduct had or was likely to have the effect of substantially lessening competition within the meaning of s.47 TPA and did not produce a net public benefit.¹⁸⁸

¹⁸⁰ Ibid at 192

¹⁸¹ Ibid at p190-191

¹⁸² Chapter 3, p58. Also above, n.152 at 194-195

¹⁸³ Above, n.158 at p582

¹⁸⁴ Ibid at p583

¹⁸⁵ F Hanks and P.L. Williams, ‘The treatment of vertical restraints under the Australian Trade Practices Act’ (1987) 15(2) ABLR 147 at 165

¹⁸⁶ Above, n.152 at p191

¹⁸⁷ The option of notification was not available to third line forcing. Above, n.185 at p147.

¹⁸⁸ Section 93(2)-(3) TPA. See also above, n.175 at p629. Pending notice from the Commission the conduct was shielded from government or third-party litigation.

3.2.1.3 Dismantling of the tied house system - *Re Tooth & Co Ltd; Re Tooheys Ltd*

In light of the foregoing, the introduction of the TPA in 1974 was a blow to the brewing industry however the dismantling of the tied house system in Australia did not occur until the late 1970s-1980s. This followed on from the Tribunal's consideration of Australian brewers' use of solus agreements. Similarly to the concerns highlighted by the Monopolies and Mergers Commission in their 1989 Report on the UK beer market,¹⁸⁹ the traditional concerns over their use have focused on their ability to raise barriers to entry at the supplier level by tying retail outlets thereby making it difficult for new suppliers to enter the market.¹⁹⁰ Where outlets are limited in number due to restrictive licensing, there has been recognition of the ability of solus agreements to consolidate and increase the market power of the brewer imposing the restrictions on retailers.¹⁹¹ At the retail level the retailer is restricted to the products of the supplying brewer thereby limiting their choice of substitutes and affecting competition at this level. As Hurly highlights these factors can cause higher prices and a restriction on the choice of goods for consumers.¹⁹²

The foregoing anticompetitive effects of solus agreements were influential in the Tribunal's judgment in *Re Tooth & Co Ltd; Re Tooheys Ltd*¹⁹³ (*Tooth*) which represented a watershed moment in the treatment of beer tie agreements in Australia. The Tribunal reviewed the ACCC's decision to refuse the grant of authorisation under s.88 TPA to brewers Tooth & Co. (*Tooth*) and Tooheys on account of the "*anticompetitive detriment*" resulting from their tying agreements.¹⁹⁴ The conduct for which they sought authorisation related to their ownership of hotels and beer production in New South Wales (NSW). More specifically this concerned their conduct and future conduct in imposing ties for the supply of bulk (draught) beer in return for the grant of leases of hotels, loans, liquor licences for hotels, and the hire of beer dispensing equipment.¹⁹⁵ The Tribunal stated that its function was to determine whether, as required under s.90(6) TPA that "*it is satisfied in all the circumstances that...the proposed conduct...would result, or be likely to result, in a benefit to the public...which would outweigh the detriment to the public...*".¹⁹⁶

¹⁸⁹ See Chapter 2.

¹⁹⁰ Above, n.167 at p337

¹⁹¹ Ibid at p337

¹⁹² Ibid at p337

¹⁹³ (1979) 39 FLR 1

¹⁹⁴ Ibid at p2

¹⁹⁵ Ibid at p2

¹⁹⁶ Ibid at p24

In the course of its considerations, similarly to the UK competition authorities in their review of tying agreements at that time discussed in Chapter 2, the Tribunal highlighted the significant influence of licensing laws in NSW.¹⁹⁷ It stated that regardless of the imposition of the tie, licensing determines the character of the distribution system by, amongst others, controlling the number and location of licensed premises.¹⁹⁸ As such it was considered to be “*the most important regulatory constraint upon the competitive functioning of the industry – with or without ties.*”¹⁹⁹ The effect of the licensing laws had generally been to restrict the number of licensed outlets in operation.²⁰⁰ The Tribunal noted that Tooth and Tooheys had the largest aggregations of licences in NSW.²⁰¹

The Tribunal also clarified the importance of market definition in the assessment of the solus agreements as barriers to entry.²⁰² It accepted that the wider the market in question the less significant the ties were as barriers to entry and as a cause of long-term anticompetitive detriment.²⁰³ The Tribunal adopted a broad approach to market definition finding that the relevant product market was beer, including bulk and packaged beer²⁰⁴ in the ‘lesser NSW market’.²⁰⁵ However market definition was not the only consideration. It found that “*the implication of the ties for both benefit and detriment needs to be considered by reference to the structure of the market in which they are embedded, the processes of competition with which they are associated, and the prospects for change.*”²⁰⁶

In considering the market structure, it was noted that whilst there was a high degree of vertical integration in the production and distribution of beer by the two brewers, the majority of the transactions involving the brewers and all retail outlets were conducted at arms’ length. Only an almost insignificant proportion of the NSW beer trade was handled by fully integrated brewer owned and managed hotels. In 1976 such outlets handled less than 1% of beer as a whole.²⁰⁷ By contrast, approximately 77% of the total beer trade was in the ‘free market’.²⁰⁸ However, here the Tribunal was concerned with the 23% of the

¹⁹⁷ Ibid at p25. NSW licensing laws were contained in the Liquor Act 1912 as amended and the Registered Clubs Act 1976 as amended.

¹⁹⁸ Above, n.193 at p26

¹⁹⁹ Ibid at p26

²⁰⁰ Ibid at p26 and p30

²⁰¹ Ibid at p32. Under the Liquor Act licences attached to premises and licences could be aggregated through the ownership of several premises.

²⁰² Ibid at p34-35

²⁰³ Ibid at p35

²⁰⁴ Ibid at p39

²⁰⁵ This referred to a region similar to, but possibly broader than the trading area of the two brewers (ibid at p43).

²⁰⁶ Ibid at p35

²⁰⁷ Ibid at p42

²⁰⁸ Ibid at p42

market in the middle ground, namely the “*the partly integrated, partly independent area*” which was the subject of the application.²⁰⁹ In considering the brewers’ tying arrangements within this category the Tribunal had regard to the competitive setting in which the ties operated. It established that at the wholesale level the NSW beer market was highly concentrated with the two brewers being the only companies brewing beer in NSW.²¹⁰ Between 1974 and 1976 they had a market share in excess of 90% of the total market for both bulk and packaged beer in NSW.²¹¹ In the same period they accounted for 95% of the NSW trade in bulk beer.²¹² Their share in packaged beer was declining but still accounted for 86% in 1976.²¹³ However, Tooth was the more powerful of the two brewers accounting for almost double the quantity of beer supplied by Tooheys in 1976 and holding almost 75% of the tied market in bulk beer.²¹⁴ The remainder of the NSW trade was accounted for by five interstate brewers.²¹⁵ At the retail level, the market was also concentrated with the two brewers’ ties and ownership links forming two significant hotel chains.²¹⁶ The ACCC had established that as at 1977 Tooth and Tooheys together owned or tied in some way 1,249 of the 1,980 hotels operating in NSW accounting for approximately 63% of these.²¹⁷ Brewers owned 37% of all hotels in NSW.

The length of the tying agreements entered into by the brewers varied from a few years to in excess of fifty or one hundred years,²¹⁸ with the lessee tie, where brewers lease their hotel to a tenant in return for guaranteed trade, being the most common form of tie.²¹⁹ However, in considering the ties in context, the Tribunal highlighted that they are “*an instrument of vertical integration*”.²²⁰ It noted that “*there are really three kinds of vertical integration between brewing and distribution to be found in this industry: (a) integration by ownership plus managerial control; (b) integration by ownership plus contract (lease and related covenants); (c) integration by contract alone (long term covenants with privately owned hotels).*”²²¹ Whilst as noted above the majority of transactions between suppliers and distributors in the beer trade were conducted at arms’ length, there was a “*highly integrated wedge of the market*”, given the high level of vertical integration in the

²⁰⁹ Ibid at p42

²¹⁰ Ibid at p57

²¹¹ Ibid at p57

²¹² Ibid at p57

²¹³ Ibid at p57

²¹⁴ Ibid at p57

²¹⁵ Ibid at p57

²¹⁶ Ibid at p58

²¹⁷ Ibid at p44

²¹⁸ Ibid at p48-49. See also above, n.158 at p594.

²¹⁹ Above, n.193 at p51

²²⁰ Ibid at p65

²²¹ Ibid at p65-66

two brewers' production and distribution of beer.²²² In the course of its consideration, the Tribunal had regard to the competitive behaviour of the brewers and established there was no obvious price competition between the two brewers in the bulk beer market and there was also little brand development or product differentiation.²²³ The tied sector was also considered to amount to a form of market sharing arrangement with the tie providing each brewer with a "*guaranteed base*".²²⁴

Under these arrangements the bulk beer sector was largely protected and within this so was the tied sector.²²⁵ The Tribunal therefore established that the agreements in question limited competition in a number of respects.²²⁶ Included amongst these was the finding that the ties prohibited the two brewers from accessing hotels already tied to the other brewer and there was no evidence of competition between them.²²⁷ They also impeded the market entry of interstate brewers by denying them access to an important segment of the market.²²⁸ The ties increased barriers to entry and so limited market entry by new brewers and hoteliers as they were restricted to acquiring an interest in a hotel with pre-determined stocking policies.²²⁹ Hoteliers' bargaining power was also limited in their dealings with the tying brewer and they were unable to obtain supplies elsewhere when their supplying brewer was unable to meet their demands. Consumer choice was also affected by these arrangements as tied hotels were restricted in their ability to change the beers they served in line with public demand.²³⁰

It was established that the 'fundamental effect' of the tie, that also gave rise to the foregoing anticompetitive effects, was its role in creating a 'captive market'.²³¹ The parties disputed the relevance of this as they claimed that only 23% of the NSW beer market was tied and so their agreements were of limited significance for market foreclosure and anticompetitive detriment.²³² The Tribunal was however satisfied that the 23% tied when considered in the context of the foregoing structural and behavioural features of the market had a significant effect upon both foreclosure and anticompetitive detriment.²³³ The Tribunal failed to be persuaded by the arguments provided regarding the public benefit. It

²²² Ibid at p66

²²³ Ibid at p74

²²⁴ Ibid at p76

²²⁵ Ibid at p79

²²⁶ Ibid at p79

²²⁷ Ibid at p79

²²⁸ Ibid at p79

²²⁹ Ibid at p79

²³⁰ Ibid at p79

²³¹ Ibid at p79

²³² Ibid at p80-81

²³³ Ibid at p81

found that neither applicant had established any benefit to the public resulting from their conduct or likely to result from it, however they were satisfied that the conduct considered had resulted and was likely to result in “*very considerable anticompetitive detriment to the public.*”²³⁴ It therefore upheld the ACCC’s decision to refuse the brewers exemption under the TPA.²³⁵

The ACCC’s decision in *Tooth* that brewers’ exclusive dealing arrangements were prohibited under the terms of the TPA heralded the start of the dismantling of the tied house system in Australia and thereby marked the end of an era for brewers. Concerns similar to those seen in the UK beer market, discussed in Chapter 2, namely the market power of brewers, barriers to entry including the role of restrictive licensing, restricted consumer choice and absence of price competition were influential in the ACCC’s decision. Following the grant of a two-week interim authorisation after the publication of the Tribunal’s reasons, brewers’ exclusivity agreements relating to mortgages, loans and covenants ceased to have effect.²³⁶ This ended brewers’ interest in hotel ownership as they pursued other ‘avenues of capital development’.²³⁷ This prohibition on the use of the beer tie combined with changing consumer preferences in favour of bottled beer had far reaching implications for the structure of the Australian brewing market similar to those examined in the context of the American market.²³⁸ As Merrett notes in 1977-1978, the four largest brewers accounted for 78% of turnover with this increasing to 92% by 1987-1988 thereby changing the market from one that was highly concentrated into a duopoly.²³⁹

3.2.2 The Competition and Consumer Act 2010

In light of the foregoing, the TPA facilitated fundamental changes in Australia’s brewing industry. The TPA was however subject to numerous reviews and debates over the coming decades. The most extensive review of its competition law provisions was conducted by the Dawson Committee Review, which made several recommendations for the technical reform of the TPA and its administration by the ACCC.²⁴⁰ The Committee’s terms of reference required it to assess whether the competition law provisions promoted competitive trading which benefitted consumers in terms of service and price. The

²³⁴ Ibid at p105

²³⁵ Ibid at p105

²³⁶ Ibid at p3

²³⁷ Above, n.127 at p148-149

²³⁸ The preference for bottled beer emerged after World War I when the Temperance movement reduced the number of hotels licensed to sell beer and reduced the hours during which sales were permitted. Above, n.125 at p239-240

²³⁹ Ibid at p243

²⁴⁰ R Steinwall, ‘The Dawson Committee Review of the competition provisions of the Trade Practices Act’ (2003) 11 C.C.L.J. 87

Committee concluded that the competition law provisions had overall served Australians well.²⁴¹ It was deemed to have achieved an appropriate balance between the prohibition of anticompetitive conduct and the promotion of competition.²⁴² While the TPA was finally replaced in 2011 by the CCA 2010, the substantive amendments were applied to fair-trading and consumer protection. The key competition provisions including s.47 TPA have been re-enacted in identical terms in the CCA 2010.²⁴³ Part VII of the CCA 2010 continues to make provision for authorisations, notifications and clearances in respect of restrictive trade practices including exclusive dealing.

3.3 The impact of outlawing the beer tie in Australia

The TPA, and now the CCA 2010, which generally outlaws exclusive dealing, together with the ACCC'S decision in *Tooth*, has had implications for the Australian beer market. The implications are not entirely dissimilar to those discussed above in relation to the 3-tier system in the US. As Dunstan highlights the beer tie in Australia was a 'tradition that dated back to the birth of the industry' and ensured the survival of many small brewers, whose tied hotels were their only outlets.²⁴⁴ Consequently, from a relatively established structure within which brewers supplied regional markets, partly on account of loyalty to local brands and partly due to high transportation costs, the Australian beer market like that in the US has evolved into a modern day duopoly. This duopoly largely divides the Australian beer market, with increasingly dominant retailers also becoming a feature of the market.²⁴⁵ In 2013, SAB Miller accounted for 43.3% of the Australian beer market by volume whilst Kirin Holdings accounted for 41.4%.²⁴⁶ By comparison, as discussed above the duopoly in the US market in 2013 was made up of ABInBev with a 50.4% market share and SABMiller accounting for 29.2% of the US market.²⁴⁷ Consequently, the Australian market is now more concentrated than the US beer market.

²⁴¹ Trade Practices Act Review Committee, 'Review of the Competition Provisions of the Trade Practices Act' at p1 (*Trade Practices Act Review*, January 2003) <<http://tpareview.treasury.gov.au/content/report.asp>> accessed 2nd July 2015. See also above, n.240.

²⁴² Trade Practices Act Review Committee, 'Review of the Competition Provisions of the Trade Practices Act' at p1 (*Trade Practices Act Review*, January 2003) <<http://tpareview.treasury.gov.au/content/report.asp>> accessed 2nd July 2015. See also above, n.240. The review will not be considered further here.

²⁴³ Above, n.164 at p379

²⁴⁴ Above, n.127 at p148

²⁴⁵ Above, n.125 at p229

²⁴⁶ Coopers Brewery Limited held the next largest market share of 6.1% whilst others held a combined market share of 9.1%. MarketLine, 'MarketLine Industry Profile Beer in Australia' (August 2014) at p12

²⁴⁷ Above, n.5 at p55

3.3.1 National brands and increased consolidation

Prior to the ACCC's decision in *Tooth* in 1979, which resulted in beer tie agreements in Australia ceasing to have effect, there was only limited competition on a national scale within the Australian beer market.²⁴⁸ Competition was generally concentrated within each State on account of both loyalty to local brands and the high transportation costs associated with shipping beer.²⁴⁹ The level of competition within individual states tended to vary from a monopoly to duopoly with only limited competition being presented by producers in neighbouring states.²⁵⁰ However the structure of the beer market changed significantly following the dismantling of the tied house system. As Merrett highlights, for the first time in decades, brewers had the ability to take market share from each other.²⁵¹ They duly did so by taking advantage of the increased consumer preference for packaged beer by switching from draught to bottled beer and transporting their products interstate.²⁵² As brewers were no longer focused on controlling distribution outlets, wide-scale marketing of their beer brands was used as a tool to both defend market share and to enter new markets.²⁵³ In the absence of vertical integration, as in the US market, focus was placed on non-price competition.²⁵⁴ The largest barrier to entry into the Australian brewing market was now the substantial expenditure required for marketing national brands.²⁵⁵ Merrett notes that the outlays required to do so were well beyond the financial means of any small or medium sized brewery.²⁵⁶ Consequently, further consolidation ensued and national brands were a reality within the Australian beer market.

As already mentioned, this trend towards consolidation has been maintained with duopolists SAB Miller and Kirin Holdings today accounting for 84.7% of the beer market by volume.²⁵⁷ In line with the increasingly global nature of the beer industry, the two main brewers in Australia today are foreign owned. Fosters, renamed Carlton & United Brewers, is owned by SABMiller, the second largest brewer in the world which is headquartered in London. Lion Nathan is now fully owned by Kirin Holdings, a Japanese based brewer. The duopoly between these two brewers was formed in 2011 following SABMiller's takeover

²⁴⁸ Above, n.7 at para 78, p327

²⁴⁹ Ibid at para 78, p327

²⁵⁰ Ibid at para 78, p327

²⁵¹ Above, n.125 at p239-240

²⁵² Ibid at p239-240

²⁵³ Ibid at p244-245

²⁵⁴ Ibid at p244

²⁵⁵ Ibid at p245

²⁵⁶ Ibid at p245

²⁵⁷ D Richardson, 'The Liquor Industry Technical Brief No.14 August 2012' (The Australia Institute) at p4 (Fare, August 2012) <<http://www.fare.org.au/wp-content/uploads/2011/07/Australia-Institute-Report-The-Liquor-Industry.pdf>> accessed 3rd July 2015

of Fosters. Despite the significant market power of the merged firm, the ACCC found that SABMiller's acquisition of Fosters was not likely to result in a substantial lessening of competition for the supply of beer.²⁵⁸ The ACCC considered that the merged firm would face competition from Lion Nathan and competition presented by smaller producers such as Coopers, who in 2013 had a market share of 6.1% of volume, microbrewers and parallel import and control brands supplied by the main supermarkets which would act as a constraint on the merged firm.²⁵⁹ As a result, the Australian beer market is now significantly more concentrated than the UK beer market.

3.4 The fringe players in the Australian beer market

The Australian and US beer markets are therefore both categorised as duopolies, however as in the American market discussed above, the Australian craft beer sector has also enjoyed an increase in market share in recent years. The Sail and Anchor Pub brewery started in 1984 is considered to be the first successful craft brewer in Australia.²⁶⁰ However, the three main beer producers in the Australian market are SABMiller, Lion Nathan and Coopers, all of which produce full strength beer and accounted for 90.8% of the Australian beer market by volume in 2013.²⁶¹ Many small producers were casualties of the mass consolidation in the market following the outlawing of the beer tie. However recently, as in the US market discussed above, there has been a renewed desire amongst Australian consumers for greater choice than simply the duopolists' products.²⁶² This is being driven by enthusiastic craft brewers and increasingly sophisticated consumers.²⁶³ Craft brewers have created a niche in which the large brewers struggle to compete due to the differing tastes and production techniques utilised.²⁶⁴ Although craft beer only accounts for approximately 2.5-3% of the Australian beer market by volume,²⁶⁵ Deloitte note that

²⁵⁸ Australian Competition and Consumer Commission, 'ACCC not to oppose SABMiller's acquisition of Foster's Group' (*Australian Competition and Consumer Commission*, 28th September 2011)

<<http://www.accc.gov.au/media-release/accc-not-to-oppose-sabmiller's-acquisition-of-foster's-group>> accessed 3rd July 2015

²⁵⁹ Ibid. See also above, n.246 at p12

²⁶⁰ Above, n.124 at p72

²⁶¹ Above, n.246 at p13

²⁶² The Crafty Pint Home of Australian Craft Beer, 'About' (*Crafty Pint*) <<http://craftypint.com/about>> accessed 3rd July 2015

²⁶³ Deloitte, 'Craft beer- Bucking the trend in Australia, Agribusiness Bulletin' at p2 (*Deloitte*) <<http://www2.deloitte.com/au/en/pages/consumer-business/articles/craft-beer-bucking-the-trend-in-australia.html>> accessed 10th March 2015

²⁶⁴ J Smith, 'Craft Beer History in Australia' (*Craft Beer Industry Association*) <<http://www.australiancraftbeer.org.au/about-us/craft-beer-history-in-australia/>> accessed 3rd July 2015

²⁶⁵ Above, n.257 at p5

the more than 150 microbreweries operating in the market are being added to with IBIS World predicting that the industry will grow by 5% over the next five years.²⁶⁶

However, beer consumption in Australia is declining overall and is currently at a 65 year low with wine replacing beer as Australia's preferred drink.²⁶⁷ The Australian craft beer sector is therefore bucking this trend as demand for 'specialist' beers is increasing at the expense of the large 'generalist' producers.²⁶⁸ This demand for craft beer has been noted by the largest brewers who are buying their way into the craft market in order to satisfy increased consumer demand for diversification.²⁶⁹ Amongst others, Lion Nathan owns the Malt Shovel Brewery that produces craft style beers and Carlton & United Breweries produce Matilda Bay brands.²⁷⁰ The ACCC has however raised some concerns over the largest brewers misleading consumers in the marketing of their 'craft' beers.²⁷¹ Australia's largest retailers Woolworths and Coles have also turned to producing their own craft brands referred to as private labels.²⁷² Woolworths for example has a partnership with craft brewer Gage Roads Brewing Co. for the supply of its private label beers.²⁷³ Consequently the market is increasing in strength with larger companies investing greater time and resources in its development.²⁷⁴

3.4.1 The old problem of the beer tie

Whilst as noted above the Australian craft beer sector's market share is increasing there are concerns that the continued use of beer tie agreements by the largest brewers is hindering its expansion. Similarly to the UK beer market discussed in Chapter 4, this use of beer tie agreements has caused craft brewers to struggle to access Australia's draft beer sector, the equivalent to the UK's on-trade.²⁷⁵ This is a lucrative market sector and approximately

²⁶⁶ Above, n.263 at p2

²⁶⁷ Ibid at p2

²⁶⁸ K Holden and I Kingham, 'In Focus – Craft Beer' (2010) 14 Drinks Trade 40 and above, n.263 at p3

²⁶⁹ Above, n.124 at p72 and K Holden and I Kingham, 'In Focus – Craft Beer' (2010) 14 Drinks Trade 40 at p40

²⁷⁰ Above, n.124. at p72

²⁷¹ Carlton and United Breweries was forced to pay a fine and provide the ACCC with a court enforceable undertaking after it claimed its Byron Bay Pale Lager was brewed by a small brewer in Byron Bay when this was not the case. The ACCC advised other brewers to ensure they were correctly marketing and labeling their beer. Australian Competition and Consumer Commission and Australian Energy Regulator 'Annual Report 2013-14' at p72 (*Australian Competition and Consumer Commission*, October 2014) <<http://www.accc.gov.au/accc-book/prINTER-friendlY/30993>> accessed 2nd July 2015

²⁷² Coles' and Woolworths' private labels only account for approximately 1.5% of the market. Above, n.257 at p5

²⁷³ Above, n.124 at p72

²⁷⁴ K Holden and I Kingham, 'In Focus – Craft Beer' (2010) 14 Drinks Trade 40 at 40

²⁷⁵ A Ferguson and R Williams, 'Storm brewing as ACCC turns up heat on big boys of beer' (*Sydney Morning Herald*, 31st May 2014) <<http://www.smh.com.au/business/storm-brewing-as-accc-turns-up-heat-on-big-boys-of-beer-20140530-399se.html>> accessed 3rd July 2015

95% of this draft beer is produced by the duopolists.²⁷⁶ These concerns have arisen despite the fact that in contrast to the UK position, exclusive dealing including beer tie agreements is generally prohibited by s.47 CCA 2010. However as discussed above this prohibition only applies where the exclusive dealing has ‘the purpose, effect or likely effect of substantially lessening competition’. Further, the possibility of notification and authorisation by the ACCC still exists for such agreements. The beer tie may therefore be legitimately used in Australia in certain circumstances.

As in the UK beer market, due to restrictive licensing there are only a limited number of on-licensed outlets in the Australian market that brewers can supply. When combined with the global decline in beer sales, already discussed, which has also affected the Australian market, there is a competitive nature to the securing of beer ‘taps’ in on-licensed establishments such as public houses (pubs). Given that draft beer is more profitable than bottled beer and is subject to reduced level of excise tax, there is once again significant competition for market share in the draft beer market through the tying of taps in pubs.²⁷⁷ There are subsequently significant similarities in the difficulties faced by Australian and UK craft brewers seeking to secure an outlet for their draft products. As is the case in the UK beer market discussed in Chapter 4, the diversity of the craft beer sector in Australia is not fully reflected in the beers served in pubs and other retail outlets.²⁷⁸

As discussed in Chapter 4 small brewers in the UK have significant problems in accessing the tied estates of pubcos as amongst others, they are unable to match the substantial discounts on beer offered to pubcos by the largest brewers. Similarly, Australian craft brewers are often eliminated from the competition to secure beer taps in pubs as they are unable to match the generous incentives offered by the larger brewers who wield significant market power.²⁷⁹ The tying agreements favoured by Australian brewers today involve them paying a venue to supply their product on tap for a certain duration, usually a number of years. Contracts imposed by the larger brewers Lion Nathan and Carlton & United Breweries have been found to impose conditions on publicans, such as requiring the exclusive right to supply 80% or even 100% of the beer taps in the outlet in return for

²⁷⁶ Ibid at p1

²⁷⁷ Ibid at p1

²⁷⁸ Ibid at p2

²⁷⁹ Concerns over the practices of the largest brewers have been investigated by the Australian consumer group CHOICE which claims that the exclusive supply contracts of the largest Australian brewers are damaging competition. P McGrath, ‘Small brewers locked out of pubs by big corporates: Choice’ (*ABC News*, 11th February 2015) <<http://www.abc.net.au/news/2015-02-11/small-brewers-locked-out-of-pubs-by-big-corporates/6086396>> accessed 3rd July 2015. See also above, n.275 at p2.

significant volume rebates and the instillation and maintenance of those taps.²⁸⁰ These beer tie agreements therefore differ from those in the UK as they can recognise the current demand for increased consumer choice and therefore only require the right to exclusively supply a percentage of the beer taps in a particular retail outlet. By contrast, it is standard practice in the UK for complete exclusivity to be granted. This therefore marginally improves the prospects of Australian craft brewers supplying their draft products to retail outlets by comparison to their UK counterparts who can face foreclosure from tied houses on account of pubcos complete exclusivity in supplying them. Further, notwithstanding the foregoing issues faced by Australian craft brewers, it is suggested that in light of the experience on the US beer market discussed above, the position of these smaller brewers would be worsened by an absolute ban on vertical integration and exclusive dealing. This would prohibit all forms of vertical integration and beer tying agreements with on-trade establishments thereby presenting an even greater challenge to the continued growth and increasing market share of the craft beer sector. As was made apparent in the consideration of the UK beer market in Chapter 2, some acceptance of the beer tie has long enabled smaller brewers to retain their market share in a rapidly consolidating market.

3.4.2 ACCC investigation into exclusive dealing in the beer market

The struggle faced by Australian craft brewers in accessing pubs and other retail outlets has recently attracted the attention of the ACCC. As discussed above, the ACCC is charged with determining whether practices such as exclusive dealing are likely to substantially lessen competition in the market. Allan Fels, the former chairman of the ACCC highlights that given the growth in the craft beer sector these exclusive contracts relied on by the larger brewers raise significant issues under the CCA 2010.²⁸¹ Fels states that “[t]he general approach is if exclusive dealing cuts competitors, especially if it forecloses markets and keeps competitors out, it is generally unlawful.”²⁸² He therefore suggests that as craft brewers attempt to gain access to pubs and other retail outlets, the exclusive dealing arrangements in the market require significant attention by the ACCC.²⁸³ The ACCC is subsequently reported to have instigated a confidential investigation into draft brewing in Australia. This includes an investigation into the practices of Lion and Carlton

²⁸⁰ Above, n.275 at p1-2

²⁸¹ Ibid at p3

²⁸² Ibid at p3

²⁸³ Ibid at p3

& United Breweries which has been highlighted as one of the ACCC's top priorities.²⁸⁴ The urgency of the investigation has been prompted by suggestions that Lion Nathan and Carlton & United Breweries, the two duopolists on the market, have used their significant market power to force out competitors from the draft beer market.²⁸⁵ Therefore should the ACCC be satisfied that the exclusive dealing arrangements of the largest brewers caused a substantial lessening of competition, the implications may be similar to the ACCC's historic decision in *Tooth* discussed above.

3.5 The establishment of powerful retailers in the Australian beer market

Notwithstanding the aforementioned competitive implications resulting from the tying of beer taps, the general prohibition on exclusive dealing under s.47 CCA 2010 has presented additional challenges as the primary means of distributing beer in Australia is now through the off-trade sector.²⁸⁶ While this change in the distribution of beer is not solely attributable to the competition law provisions of the CCA, with this being a global trend in beer distribution and with Australian consumers exhibiting an early preference for bottled beer, there was a significant shift from draft to bottled beer in the aftermath of the ACCC's decision in *Tooth* discussed above.

As in the UK market, today the off-trade sector is mainly made up of off-licenses and supermarkets, with the latter dominating. In 2011 Citigroup estimated supermarket chains Coles and Woolworths' market share of liquor retail to be 58% and rising.²⁸⁷ These chains operate three different store formats. They operate 'big box' stores, with Woolworths and Coles stores accounting for 27% of retail liquor industry revenues; convenience stores; and specialty standalone stores.²⁸⁸ Coles and Woolworths therefore enjoy market power in the Australian off-trade. This has been the result of organic growth with acquisitions being historically significant to these companies.²⁸⁹ The influence of these chain stores however is also increased by their production of 'private' label beers that are essentially 'home

²⁸⁴ Ibid at p3. See also A Ferguson, 'Beer battle 'priority' as ACCC puts heat on Lion, Carlton & United over beer tap deals' (*Sydney Morning Herald*, 16th February 2015) <<http://www.smh.com.au/business/beer-battle-priority-as-acc-puts-heat-on-lion-carlton--united-over-beer-tap-deals-20150216-13fno0.html>> accessed 3rd July 2015

²⁸⁵ A Ferguson, 'Beer battle 'priority' as ACCC puts heat on Lion, Carlton & United over beer tap deals' (*Sydney Morning Herald*, 16th February 2015) <<http://www.smh.com.au/business/beer-battle-priority-as-acc-puts-heat-on-lion-carlton--united-over-beer-tap-deals-20150216-13fno0.html>> accessed 3rd July 2015

²⁸⁶ Datamonitor, 'Australian Beer Market Profile 2002'

²⁸⁷ A Bowley on behalf of Citigroup, 'Living with the Chain Stores' at p134 (*The Drinks Trade*, October - November 2011) <[http://www.drinkstrade.com.au/ContentFiles/Documents/Drinks Trade/Public/Library/reports/retailer/Issue 25 Oct-Nov 11 Living with the Chain Stores Citigroup Thirsty Thoughts reports liquor retail market backdrop.pdf](http://www.drinkstrade.com.au/ContentFiles/Documents/Drinks%20Trade/Public/Library/reports/retailer/Issue%2025%20Oct-Nov%2011%20Living%20with%20the%20Chain%20Stores%20Citigroup%20Thirsty%20Thoughts%20reports%20liquor%20retail%20market%20backdrop.pdf)> accessed 3rd July 2015

²⁸⁸ Ibid at p135

²⁸⁹ Ibid at p134

brands'.²⁹⁰ This was exemplified by Woolworths' acquisition of a 25% stake in craft brewer Gage Roads Brewing Co. which enabled it to secure volumes to supply its private label.²⁹¹ It has been reported that Coles' private label sales constitute 20% of their total sales with this continuing to strengthen. One of its private labels produced by brewer Independent Distillers, is outselling branded beer competitors.²⁹² Bowley however highlights some of the implications of supermarket chains producing their own private labels. These include the fact that chain stores are most likely to prioritise shelf space to the advantage of their own labels; they are able to replicate producer led innovation; and chain stores secure even greater bargaining power against producers.²⁹³ Bowley also notes that their continued success lies in the fact that price is the principle differentiator in chain store retailing.²⁹⁴ Chain stores are able to use their favourable trading terms and efficient supply chains to offer low cost options.²⁹⁵ Brewers have however expressed concerns that the increasing margin pressure from national retailers presents a challenge to the industry going forward as this limits their ability to invest in product development and new capital equipment.²⁹⁶ The imbalanced bargaining power between supermarkets and suppliers, which is partially attributable to the low switching costs for supermarkets, has also attracted the attention of the ACCC.²⁹⁷ Supermarket practices have been highlighted as including the placing of unreasonable demands on suppliers and threatening product removal, as well as favoring their home brand products to the detriment of suppliers.²⁹⁸ Consequently politicians in Australia have called for legislation to bring about divestiture within the supermarket sector.²⁹⁹

²⁹⁰ Supermarket production of private labels often involves the use of contract brewers who are responsible for their recipe, development and marketing. They allude to a fictional brewery as part of the marketing scheme. By contrast, home brands carry the name of the producing supermarket and are not as marketable as private labels. For example, Gage Roads Brewing Co. produces Woolworths' private label Sail & Anchor. See J Bird, 'Craft Beer who owns your favourite Australian boutique brew?' (*Choice*, 8th August 2014) <<https://www.choice.com.au/food-and-drink/drinks/alcohol/articles/craft-beer-who-owns-your-favourite>> accessed 12th March 2015. The Brewers Association, 'Market Segments' (*The Brewers Association*) <<http://www.brewersassociation.org/statistics/market-segments/>> accessed 3rd July 2015

²⁹¹ A Ferguson, 'Bitter Battles in what looks to be an ailing market' (*The Sydney Morning Herald*, 9th February 2013) <<http://www.smh.com.au/business/bitter-battles-in-what-looks-to-be-an-ailing-market-20130208-2e3wx.html>> accessed 3rd July 2015. Above, n.287 at p136.

²⁹² A Ferguson, 'Bitter Battles in what looks to be an ailing market' (*The Sydney Morning Herald*, 9th February 2013) <<http://www.smh.com.au/business/bitter-battles-in-what-looks-to-be-an-ailing-market-20130208-2e3wx.html>> accessed 3rd July 2015

²⁹³ Above, n.287 at p135

²⁹⁴ Ibid at p135

²⁹⁵ Ibid at p135

²⁹⁶ Concerns have also been expressed regarding the impact of retailer consolidation on the beer market going forward. See above, n.274 at p43-44

²⁹⁷ B Fragos, 'Australia: competition - compliance and enforcement' (2014) 25(9) I.C.C.L.R. N53 at N54 and above, n.246 at p17

²⁹⁸ B Fragos, 'Australia: competition - compliance and enforcement' (2014) 25(9) I.C.C.L.R. N53 at N54

²⁹⁹ Ibid at N53-N54

3.6 Australian approach is not a solution to the challenges faced in the distribution of beer in the UK market

In light of the foregoing it is clear that Australia has not gone as far as the US in outlawing the beer tie as an illegitimate business model in all circumstances. It has however adopted a stricter approach than the UK where, under the influence of the EU, the tie generally benefits from reciprocal exemption under Regulation 330/2010³⁰⁰ without the need for notification to the European Commission. Where such exemption is not available, the Chapter I prohibition of the Competition Act 1998 must be breached before the conduct is prohibited. As noted above, this imposes a higher test than that of s.47 CCA 2010 which generally prohibits all exclusive dealing such as the beer tie where it has the purpose effect or likely effect of substantially lessening competition.³⁰¹ This is so even although the newly adopted 2015 Act restricts the operation of the beer tie in the UK by requiring large pub owning businesses to offer their tied tenants a MRO option in certain circumstances as discussed in Chapter 4.

As shown above this stricter approach by the Australian competition authorities has not had an entirely positive effect on the competitive situation in the Australian beer market suggesting that it is not a suitable model for the UK market to follow. After the introduction of s.47 TPA and the Tribunal's decision in *Tooth*, the Australian brewing market has transformed from a relatively fragmented market into a national duopoly today. The two largest producers Lion Nathan and United & Carlton Brewers in 2013 enjoyed a combined market share of 85.7% which is even greater than that of the US duopolists discussed above. Consequently, the Australian approach to regulation of their beer market has caused, amongst others, increased concentration, a reduction in consumer choice and an increase in barriers to entry although it has not produced an equivalent to the pubco.

Australian consumers have however recently begun to enjoy greater variety beyond the dupolists' generic products as the country's craft beer sector has gained market share amidst increased consumer demand for choice in the beer market. This growth has occurred under a legal regime that in contrast to the US market allows for some acceptance of vertical integration and reliance on the beer tie, again suggesting that the UK market should not be regulated in a way that prohibits this outright. Nevertheless, as in the UK beer market, the increased diversity resulting from these developments is not necessarily reflected in the range of products offered in Australia's pubs and other on-trade outlets.

³⁰⁰ See Chapter 4.

³⁰¹ Section 47(10) CCA 2010

This is also due to the continuing use of beer tying agreements by the largest brewers with this practice reportedly undergoing investigation by the ACCC. However, in certain cases, the range of beers offered in tied establishments is not as restricted as it is in the UK due to the use of tap contracts that only require a certain proportion of the pub's taps be tied to that brewer, although in some cases 100% exclusivity is demanded. Therefore, whilst there are undoubtedly consequences associated with the use of beer tie agreements by the largest brewers, in light of the implications of the outright prohibition on exclusive dealing in the US market which largely precluded the development of any brewing sector to rival the largest players, some acceptance of exclusive dealing is still preferable to outlawing this entirely.

Nevertheless, a further implication of the Australian approach to exclusive dealing is that off-trade beer sales have long been greater than those through the on-trade. Whilst the switch to off-sales of beer is now a trend in the global beer market, similarly to the US market, this was expedited in Australia due to the general prohibition on exclusive dealing. Today powerful supermarket chains Woolworths and Coles are well established and now dominate off-trade sales in Australia. Although their success has been greatly influenced by their ability to offer consumers low cost options, as discussed above, their development of private labels and significant bargaining power in dealings with suppliers potentially has implications for the beer market going forward with their practices also attracting the attention of the ACCC. Therefore the potential for reforms to the UK's regulation of the beer market to increase the role of supermarkets in the distribution of beer should be acknowledged when making recommendations for reform.

In light of the foregoing, despite Australia's stricter approach to the beer tie than that in the UK, the Australian market is more concentrated and similarities can be drawn between the competitive concerns in both over the use of beer tying agreements today. Therefore regard will be had to the arrangements for the distribution of beer in Belgium where the tie is permitted under a competition law regime that is largely similar to that in the UK, however the beer market is considered to be one of the most diversified in the World.

4. The Belgian beer market

Belgium, despite its small geographical size, is one of the world's major beer producers and is home to a significant variety of beers. On a *per capita* basis this is higher than any

other country.³⁰² It is also the birthplace of the world's largest brewer Anheuser Busch InBev (AB InBev), whose roots can be traced back to the 14th Century. Today it operates alongside many Belgian brewers with a similarly impressive history which utilise traditional techniques but compete in the global marketplace.³⁰³

4.1 A brief history of the Belgian beer market and the role of the tie

Brewing is said to be “*ingrained in the culture*” in Belgium, having been introduced by the Romans.³⁰⁴ Several factors have however influenced the rich variety of Belgian beers produced today.³⁰⁵ Being embedded amongst France, Germany and the Netherlands, and having had Europe's leading forces take charge of the country at various points in time, has influenced the flavours and techniques employed in brewing in Belgium.³⁰⁶ As a result these are considered to be probably the most varied in the world.³⁰⁷ Oliver highlights that many of these techniques continue to be used today, providing inspiration to brewers all over the World.³⁰⁸ Religious institutions, such as monasteries, have also engaged in the production of beer thereby adding to this diversity.³⁰⁹ By the early 20th Century, Belgium enjoyed the beer of over three thousand commercial breweries and in contrast to most other European countries, including the UK, these beers were enjoyed by all social classes due to the significant import duties on French wine.³¹⁰

This diversity endured and by World War I the market was still highly fragmented. Due to the relatively low start-up costs for brewers relative to the high transportation costs for beer, small local brewers dominated.³¹¹ These local beers had their own distinctive tastes, making market integration difficult.³¹² However Van Der Hallen notes that due to wartime restrictions the Belgian beer market began to consolidate and although consumption levels recovered in the post-war era, the number of breweries in operation did not.³¹³ During World War I many Belgian breweries were stripped of their copper equipment and several

³⁰² D Persyn, J.F.M. Swinnen and S Vanormelingen, ‘Belgian beers: where history meets globalization’ in J.F.M. Swinnen, eds, *The Economics of Beer* (New York, Oxford University Press Inc., 2011) at p79

³⁰³ Ibid at p79-80

³⁰⁴ The Economist, ‘Belgian Beer Brewed Force’ (*The Economist*, 17th December 2011) <<http://www.economist.com/node/21541708>> accessed 3rd July 2015

³⁰⁵ It has been estimated that Belgium produces 1,131 beers (ibid at p2).

³⁰⁶ Above, n.124 at p120

³⁰⁷ Ibid at p120. See also Horst Dornbusch ‘Belgium: a Brew Melting Pot’ (*Beer Advocate*, 27th October 2004) <<http://beeradvocate.com/articles/611>> accessed 3rd July 2015

³⁰⁸ Above, n.124 at p120

³⁰⁹ Ibid at p120

³¹⁰ Above, n.304 at p4

³¹¹ P Van der Hallen, (2009) ‘Concentration in the Belgian brewing industry and the Breakthrough of lager in the interwar years’ KU Leuven CES Discussion Paper 07.28 at p9-10. See also, n.304 at p4

³¹² P Van der Hallen, (2009) ‘Concentration in the Belgian brewing industry and the Breakthrough of lager in the interwar years’ KU Leuven CES Discussion Paper 07.28 at p10

³¹³ Ibid at p10 and p14

were destroyed.³¹⁴ German occupation during the war is also thought to have introduced lager-type beers to the Belgian market. This was a more homogeneous product than locally brewed beers with their specific production techniques. Lager therefore made it possible for brewers to penetrate the markets of rival brewers.³¹⁵ The introduction of lager combined with a reduction in transportation costs, due to improvements in the road network and the use of motorised vehicles, resulted in rapid consolidation of the Belgian beer market in the inter-war years and beyond.³¹⁶

4.1.1 Brewers' reliance on beer tying agreements

This consolidation posed a threat to small and medium sized brewers operating in the Belgian beer market. They were forced to defer to traditional means to defend their market share including placing increased reliance on the use of the beer tie. Similarly to brewers in the UK, discussed in Chapter 2, the tie had long been relied on by Belgian brewers due to the perishable nature of their traditional beers and the need for reliable outlets for their products.³¹⁷ However, in the late 1920s the largest brewers sought to capitalise on this when it became apparent that the smallest brewers in the Belgian market lacked the resources to produce their own lager beers which were increasing in popularity. Van Der Hallen notes that they did so by offering these smaller brewers their brands at a discount.³¹⁸ Many brewers accepted this offer and sold the lager brands of the largest brewers alongside their own traditional beers.³¹⁹ As customers increasingly opted for the lager on offer many small brewers eventually opted to exclusively sell the larger brewers' brands from their retail outlets.³²⁰ Nevertheless, as medium sized brewers continued to lose market share they increasingly relied on beer tie agreements with pubs and offered outlets credit or other financial advantage in return for purchasing their products to the exclusion of their competitors' products.³²¹ However, for the same reasons that have influenced the widespread use of the tie in the UK discussed in Chapter 2, Van Der Hallen notes that the larger brewers also relied heavily upon the beer tie when consumption levels began to decline in the 1930s.³²² Brewers were concerned that declining beer consumption would result in the under utilisation of production capacity.

³¹⁴ Above, n.124 at p120

³¹⁵ Above, n.312 at p23

³¹⁶ Ibid at p23. Also above, n.302 at p80-81

³¹⁷ Above, n.312 at p29

³¹⁸ Ibid at p28

³¹⁹ Ibid at p28

³²⁰ Ibid at p28

³²¹ Ibid at p29

³²² Ibid at p29

Whilst this widespread use of the tie initially had the desired effect, in that all brewers managed to secure their market share to some degree or another, smaller brewers soon ran into difficulty as tying distribution channels in this way was costly.³²³ As their capital was tied up it could not be used to improve their products and ultimately they could not compete with the favourable enticements offered by the largest brewers. Over the coming decades, this prompted the exit from the market of many smaller brewers.³²⁴ The market therefore consolidated further with the remaining brewers competing by taking over the distribution networks of their rivals with this increasing greatly after World War II.³²⁵ The ensuing mergers remained a feature of the market throughout the coming decades as did the use of the beer tie and loan tying agreements.³²⁶

Consequently the UK and Belgian beer markets have placed similar reliance on the beer tie throughout their histories. However, Van Der Hallen also distinguishes these two markets by acknowledging the role restrictive licensing played in shaping the UK market.³²⁷ There was no parallel to restrictive licensing in operation in Belgium at that time and so the use of tying agreements had different effects on the structure of the Belgian and UK markets.³²⁸ As licensing laws restricted the number of retail outlets available to brewers in the UK, the structure of the market was largely frozen unless a merger between brewers occurred. Van Der Hallen therefore suggests that the combination of restrictive licensing and the tied house system served to preserve some fragmentation within the UK market up until the 1950s.³²⁹ By contrast, the number of outlets in Belgium at that time was unconstrained by such licensing requirements and the Belgian Government adopted a more lax approach towards mergers than in the UK. The evolution of the Belgian market was therefore less constrained than in the UK with further consolidation resulting.³³⁰

³²³ Ibid at p30

³²⁴ Ibid at p30

³²⁵ Ibid at p30

³²⁶ Above, n.7 at para 12, p313

³²⁷ Above, n.312 at p31

³²⁸ Ibid at p31

³²⁹ Ibid at p31. See also G Johnson and H Thomas, 'The Industry Context of Strategy, Structure and performance: the UK Brewing Industry' (1987) 8 Strategic Manage J, 343 at 344

³³⁰ Belgian licensing policy is now a Federal matter. All retailers of alcoholic beverages require a licence to operate. E Österberg and T Karlsson, (eds), 'Alcohol policies in EU Member States and Norway A Collection of country reports' (*Europa*, 1998)

<http://ec.europa.eu/health/ph_projects/1998/promotion/fp_promotion_1998_a01_27_en.pdf> accessed 3rd July 2015. Above, n.312 at p31.

4.1.2 Consolidation in the Belgian beer market and increased exports in the Belgian beer market

Belgium became a founding member of the EU in 1957 and the beer tie remained as prevalent throughout the 1950s and 1960s in the absence of any restrictions on this practice or that of granting credit to outlets.³³¹ As a result, by the 1960s following a series of take overs, the Belgian brewer Artois had established itself as the largest in the country. Given Belgium's long acceptance of the beer tie, by 1961 it was estimated that 81% of Belgium's restaurant, hotel and café (horeca) sector, was tied in some way to a brewery.³³² Nevertheless, in keeping with the global trend of declining beer consumption, Belgian brewers were also forced to explore the possibility of international expansion.³³³ As this strategy was successful, by the 1970s decreased reliance was placed on tying regional distribution networks. Although the practice did not disappear, by relaxing this system there was a reduction in the costs incurred by brewers in operating their regional networks.³³⁴ As in the US and Australian beer markets discussed above, marketing became an increased source of expenditure for brewers at this time.³³⁵ Consequently, Houthoofd and Heene highlight the tied house system, strong brand recognition and reputation, as well as significant capital expenditure on, amongst others, advertising and promotion became significant barriers to entry to the largest sector of the beer market, namely the pils (lager) segment.³³⁶ This was not however the case in the non-pils segment of the Belgian market. There beers were still produced on a smaller scale with larger production costs. These traditional production techniques, whilst costly, introduced differentiation that offset the differentiation amongst the large pils producers brought about by extensive marketing of their brands and made these smaller brands desirable to consumers.³³⁷

Nevertheless, as Belgian brewers looked to exploit the opportunities presented by international expansion, by 1990 approximately 10% of Belgian beer production was marked for export.³³⁸ This has increased to over half of the total beer produced in Belgium

³³¹ Above, n.312 at p31. This was also the case in the 1980s-1990s. Above, n.7 at para 12, p313

³³² Above, n.312 at p30-31

³³³ Ibid at p31

³³⁴ Ibid at p31

³³⁵ Ibid at p31

³³⁶ N Houthoofd and A Heene, 'Strategic groups as subsets of strategic groups in the Belgian brewing industry' (1997) 18(8) Strategic Manage J 653 at 655

³³⁷ Ibid at p655

³³⁸ M Brink et al, 'The contribution made by beer to the European Economy' at p60 (Ernst & Young, 2011) (*The Brewers of Europe*) <[http://www.brewersofeurope.org/uploads/mycms-files/documents/archives/publication\(1\).pdf](http://www.brewersofeurope.org/uploads/mycms-files/documents/archives/publication(1).pdf)> accessed 2nd July 2015. See also n.302 at p80

today, making it Europe's second largest exporter of beer.³³⁹ In addition to developing this export market for Belgian beer, Belgian brewers were ahead of the trend in international consolidation and rapidly started to acquire their foreign counterparts. This foresight resulted in InBev, the world's largest brewing company being a Belgian based brewer.³⁴⁰ In 2008, InBev acquired America's largest brewer Anheuser Bush (AB), to form AB InBev, reinforcing its position as the largest brewer in the world.³⁴¹ However, in line with being home to the world's largest brewer, despite the diversity of beers brewed in Belgium today the Belgian beer market is now highly concentrated. In 2013 AB InBev accounted for 53.9% of the Belgian beer market by volume, with the three largest Belgian brewers having a combined market share of 76.3% of the market by volume.³⁴² Whilst highly concentrated, the top two producers had a combined market share of 71% thereby still comparing favourably to the duopoly in the US market discussed above where the top two brewers have a combined market share of 79.6% of the US beer market by volume in 2013.³⁴³ Similarly, this is also favourable to the Australian duopolists' market share of 84.7% of the Australian beer market by volume in 2013.³⁴⁴ All three markets are however significantly concentrated by comparison to the UK beer market discussed in Chapter 4 where the three largest producers had a combined market share of 71.6% of the UK beer market by volume in 2013.³⁴⁵ The Belgium beer market is however closer to the UK market's level of concentration than the US and Australian markets.

4.2 Legal acceptance of the beer tie

Notwithstanding the foregoing developments in the Belgian beer market that have decreased Belgian brewers' dependence on tying domestic distribution networks, similarly to the UK market discussed in Chapter 4, the beer tie is still an important business model used by Belgian brewers. This reliance was initially unaffected by Belgium's membership of the EU in 1957. Whilst Articles 101 and 102 TFEU were applicable in certain Belgian

³³⁹ In 2012 Belgium was the second largest exporter within the EU after the Netherlands. Berkhaut B et al, 'The contribution made by beer to the European Economy' at p74 (*Ernst & Young*, 2013)

<[http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/\\$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf](http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf)> accessed 2nd July 2015. Also, above, n.302 at p80

³⁴⁰ In 1995, InBev, then known as Interbrew, acquired Canadian based Labatts and in 1995 proceeded to merge with Brazilian based AmBev to create the world's largest brewer InBev in 2004. Above, n.304 at p4

³⁴¹ Above, n.304 at p4

³⁴² Heineken N.V. has a market share of 17.1% by volume followed by Haacht N.V. with 5.3%. 'MarketLine Industry Profile Beer in Belgium' (August 2014) at p12

³⁴³ Ibid and above, n.58 at p12

³⁴⁴ Above, n.246 at p12

³⁴⁵ Above, n.59 at p12. By comparison, the top three producers in the US had a combined market share of 85.6% (above, n.58 at p12), in Australia 90.8% (above, n.246 at p12) and in Belgium 76.3% (above, n.342 at p12).

competition law cases due to their direct effect and their supremacy over national law, Belgium lacked its own competition laws and policy. This was with the exception of an under utilised Act of the 1960s which dealt with the abuse of economic power.³⁴⁶

4.2.1 The Competition Act 1991

Belgium's first substantive competition law provisions did not come into force until the introduction of the Competition Act 1991 (the 1991 Act).³⁴⁷ As with the UK's Competition Act 1998 discussed in Chapter 4, this sought to implement a national competition law regime that was aligned with the EU competition law provisions.³⁴⁸ As this was based on EU competition law, the terms of Articles 101 and 102 TFEU were clearly reflected in the provisions of the 1991 Act that detailed the prohibited conduct. Article 2 of the 1991 Act dealt with restrictive practices with the object or effect of preventing, restricting or materially distorting competition in the relevant Belgian market or a substantial part of it; and Article 3 attended to abuses of dominance in the relevant Belgian market or a substantial part of it. The main difference from the EU provisions was therefore the 1991 Act's focus on the Belgian market and the lack of a requirement for an inter-state effect. The Belgian Supreme Court also made clear its intention to interpret and apply its provisions in line with EU law.³⁴⁹ However, in 2006 the 1991 Act was replaced by two Acts³⁵⁰ that were subsequently consolidated into a single Royal Decree. This was the Belgian Act on the Protection of Economic Competition 2006 (the 2006 Act).³⁵¹

³⁴⁶ Act of 27 May 1960 on protection against the abuse of economic power. Y Montangie, 'The Application of EU Competition Law by the Belgian Competition Authorities and Judges: Is Belgium Prepared for the "New Regime"?' (2004) 1 (1) *The Competition Law Review* 41 at 42

³⁴⁷ Act of 5 August 1991 which came into force on 1st April 1993. Organisation for Economic Cooperation and Development 'Belgium (2001)' at p3 (OECD, 2001) <<http://www.oecd.org/belgium/2489009.pdf>> accessed 3rd July 2015. See Y Montangie (2004) 1 (1) *The Competition Law Review* 41 at p42.

³⁴⁸ I.M. Rahman and W Vandenberghe, 'Handbook on Multijurisdictional Competition Law Investigations' (*American Bar Association*) <<http://www.dechert.com/files/Publication/09ed0825-70be-4f59-b8bb-72cf593b22a4/Presentation/PublicationAttachment/73c5c60f-5ada-462b-a35c-851a15522eed/Belgium%20Multijurisdiction%20Competition%20Law%20Investigations%20-%20ABA%20Multijurisdiction%20Handb.pdf>> accessed 3rd July 2015 and Y Montangie (2004) 1 (1) *The Competition Law Review* 41 at p42

³⁴⁹ Y Montangie, 'The Application of EU Competition Law by the Belgian Competition Authorities and Judges: Is Belgium Prepared for the "New Regime"?' (2004) 1 (1) *The Competition Law Review* 41 at p43 citing Hof van Cassatie [Supreme Court], decision of 9 June 2000 ('Trade Mart'), (2000) *Arr Cass*, p354 (Reported in French or Dutch)

³⁵⁰ The Protection of Economic Competition Act of June 10 2006, *Moniteur Belge*, June 29, 2006, 32,755 detailed the Belgian competition law provisions. The second Act was The Establishment of a Competition Authority Act of June 10, 2006, *Moniteur Belge*, June 29, 2006, 32,746 which established the Competition Authority.

³⁵¹ Belgian Act on the Protection of Economic Competition of September 15 2006, *Moniteur Belge*, September 29, 2009, 50, 613 Consolidated on 15th September 2006 (Belgian Official Gazette 29/9/2006) and amended by the Act of 6/5/2009 (Belgian Official Gazette 19/5/2009) <http://economie.fgov.be/en/binaries/apec-new_tcm327-56301.pdf> accessed 18th March 2015. The official translation is in Dutch or French.

4.2.2 Act on the Protection of Economic Competition 2006 and its successors

The main prohibitions contained in the Competition Act 1991 were reflected in Chapter II of the 2006 Act which dealt with anti-competitive practices. Similarly to the 1991 Act, Article 2(1) of the 2006 Act was the equivalent of Article 101 TFEU prohibition, while Article 3 reflected Article 102 TFEU.³⁵² Article 5 of the 2006 Act also confirmed the benefit of the EU block exemption regulations to restrictive practices, with this extending to situations where there was no effect on inter-state trade and so only the Belgian market was affected.³⁵³ Consequently the 2006 Act was very similar in its terms to the UK's Competition Act 1998, discussed in Chapter 4. While the 2006 Act failed to define 'vertical restraint' or to provide examples of the conduct affected, as noted above Belgian competition law was to be interpreted in accordance with EU jurisprudence. The Competition Council and its auxiliary bodies had primary responsibility for the administrative enforcement of the Belgian competition law rules.³⁵⁴ However, Montangie states that it "*malfunctioned from the outset*".³⁵⁵

The Competition Council was therefore soon replaced. Two Acts of April 13, 2013 were implemented in place of the 2006 Act with new competition rules also being integrated into the new Code of Economic Law.³⁵⁶ The substantive competition law provisions are now detailed in Book IV of the Code of Economic Law (CEL).³⁵⁷ Whilst this introduced

³⁵² Article 3 will not be considered any further here.

³⁵³ Above, at n.351

³⁵⁴ Y Montangie, 'The Application of EU Competition Law by the Belgian Competition Authorities and Judges: Is Belgium Prepared for the "New Regime"?' (2004) 1 (1) The Competition Law Review 41 at p44

³⁵⁵ The problems included the fact the Competition Council was under-resourced to deal with its workload (ibid at p44-47). The Council was also criticised for its lack of economic analysis in competition cases (ibid at p49).

³⁵⁶ Wet 13 April 2012 houdende invoeging van boek IV "Bescherming van de mededinging" en van boek V "De mededinging en de prijsevoluties" in het Wetboek van economisch recht en houdende invoeging van de definities eigen aan boek IV en aan boek V en van de rechtshandhabingsbepalingen eigen aan boek IV en aan boek V, in boek I van het Wetboek van economisch recht, *Belgian Official Journal April 26, 2013*; Wet 13 April 2013 houdende invoeging van de bepalingen die een aangelegenheid regelen als bedoeld in artikel 77 van de Grondwet, in boek IV "Bescherming van de mededinging" en boek V "De mededinging en de prijsevoluties" van het Wetboek van economisch recht, *Belgian Official Journal April 26, 2013*. See C Cauffman 'Competition litigation in Belgium and Luxembourg between 2000 and 2012' (2014) 7(1) Global Competition Litigation Review 39 at 40.

³⁵⁷ Also referred to as the Competition Act of 3 April 2013 (Belgian Official Gazette 26-4-2013). Unofficial English translation available at

<http://economie.fgov.be/en/binaries/Book_IV_of_the_Code_of_Economic_Law-The_Act_english_translation_tcm327-241692.pdf> accessed 19th March 2015

significant reforms to the Belgian Competition Authority, the substantive provisions regarding anti-competitive practices described above remain unchanged.³⁵⁸

As was the case under Article 2 of the 2006 Act, Article IV.1 of the CEL is equivalent to Article 101(1) TFEU and is subsequently also very similar to the UK's Chapter I prohibition in the Competition Act 1998. This states that 'all agreements between undertakings, all decisions by associations of undertakings and all concerted practices, the aim or consequence of which is to prevent, restrict or distort significantly competition in the Belgian market concerned or in a substantial part of that market are prohibited'.³⁵⁹ It is therefore applicable to brewers' exclusive dealing agreements. Agreements or decisions coming within this provision are automatically void under Article IV.1(2) CEL. However, reflecting the terms of Article 101(3) TFEU, discussed in Chapter 3, the possibility of exemption from the prohibition is offered under Article IV.1(3) CEL. This has been extended further than Article 101(3) TFEU by adding to the exemption criteria "*any concerted practice...which enable small and medium sized undertakings to assert their competitive position in the market concerned or internationally*".³⁶⁰ Therefore, in keeping with the EU competition law provisions, Belgian competition law is more concerned with the interests of consumers, small and medium sized undertakings and efficiency gains when granting exemptions to prohibited anticompetitive practices than their Australian counterparts under the CCA 2010 discussed above.

Similarly to the 2006 Act, whilst no definition of vertical restraint is provided in the CEL, as already mentioned Belgian law is to be interpreted in line with EU law. Therefore the types of restraint caught are largely identical to those under the EU competition law provisions discussed in Chapter 3. Further, Article IV.4 CEL confirms that the Belgian competition provisions are inapplicable to agreements benefitting from EU block exemption Regulations with this also extending to arrangements lacking any inter-state effect. In light of this, block exemption Regulation 330/2010 discussed in Chapter 3 is applicable to beer tie agreements that only have an effect on the Belgian market. The Belgian competition law regime is therefore very similar to the UK's competition law regime discussed in Chapter 4 and reflects the EU position that the beer tie agreement

³⁵⁸ The principal changes brought about in 2013 were of a procedural and institutional nature. The intention was to streamline the Belgian institutional structure through the establishment of a new independent Competition Authority thereby also increasing efficiency. See ECN Brief May 2013 at p33 <http://ec.europa.eu/competition/ecn/brief/02_2013/brief_02_2013_short.pdf> accessed 3rd July 2015 and C Cauffman, 'Competition litigation in Belgium and Luxembourg between 2000 and 2012', (2014) 7(1) Global Competition Litigation Review 39 at 40

³⁵⁹ Article IV.1(1) CEL

³⁶⁰ Article IV.1(2)(3) CEL

constitutes a legitimate business model. However, like their UK counterparts the extensive use of the beer tie by Belgium's largest brewers has long attracted the attention of the European competition authorities as exemplified by the 1967 *Brasserie de Haecht* case, discussed earlier in Chapter 3.³⁶¹

4.3 European Competition Authorities scrutiny of Belgian brewers' practices

The beer tie has been and continues to be used widely in the Belgian and UK beer markets. However, as mentioned above, given the ability of such exclusive agreements to foreclose markets and aid the acquisition of market power, brewers' reliance on such agreements has been subject to regular scrutiny by the European competition authorities.³⁶² Therefore although EU membership initially had little practical impact on the practices of Belgian or UK brewers, this changed in 1999 with the adoption of the new Block Exemption Regulation 2790/99.³⁶³ As discussed in Chapter 3, this made exemption of such agreements conditional on compliance with a new market share requirement. Article 3 of Regulation 2790/99 imposed a market share cap of 30% as a condition for exemption from the EU competition law provisions. Prior to this, in the absence of any market share threshold, Belgian brewers had largely enjoyed a free rein to tie as many outlets as they desired.

4.3.1 AB InBev's use of beer tie agreements

The adoption of the market share approach under Regulation 2790/99 prompted Belgium's largest brewer AB InBev, then called Interbrew, to notify the European Commission in June 2000 of its supply agreements with on-trade establishments in Belgium.³⁶⁴ At the time of notification, AB InBev held a market share of approximately 56% of the Belgian horeca sector whilst the second largest brewer Alken Maes had a market share of only 13%.³⁶⁵ AB InBev was therefore the only Belgian brewer at that time not to qualify for exemption under Regulation 2790/99 on account of its market share.³⁶⁶ The Commission noted that of the 52,000 horeca outlets operating in the Belgian market, 35,000 were pubs. Over 20,000 of these sold AB InBev's beers with 11,000-13,000 being subject to an exclusive supply agreement.³⁶⁷ Of those tied to AB InBev, over 7,000 were subject to loan tie agreements

³⁶¹ Chapter 3, p61

³⁶² See Chapter 3.

³⁶³ (1999) OJ L336/21

³⁶⁴ *Interbrew* ((2002) OJ C283/14)

³⁶⁵ *Ibid* at para 7, p14

³⁶⁶ K Atsma, 'European Commission opens up Interbrew's Belgian Horeca outlets to competing beer brands' (2003) (2) ECCPN 58 at 58

³⁶⁷ Above, n.364 at para 8, p14

and over 3,000 were subject to lease or sublease tie agreements, all with a requirement to exclusively supply the brewer's products.³⁶⁸ The loan tie agreements were subject to a maximum duration limit of 5 years.³⁶⁹ In accordance with Belgian law, the lease ties were generally concluded for a period of 9 years and were renewable for a further 9 years up to a maximum duration of 27 years.³⁷⁰

In order to secure exemption for its agreements AB InBev proposed certain concessions. The Commission subsequently imposed further demands on the brewer before it accepted that their supply agreements did not restrict competition in an appreciable manner.³⁷¹ The extent of the tie imposed under the notified agreements varied. AB InBev's loan tie agreements were divided into two categories, both imposing different tying obligations. Firstly, contracts entered into after 1 March 2001 imposed a non-compete obligation in respect of draft beer only, thereby excluding bottled and canned beers and other drinks.³⁷² Those entered into from 1 June 2001 were terminable annually on 3 months' notice.³⁷³ Secondly, those loan agreements entered into after 1 July 2001 had this non-compete obligation replaced with a minimum-purchasing obligation requiring 75% of total beer turnover to be purchased from AB InBev.³⁷⁴ Under the concessions granted the outlets tied by loan agreement had their minimum-purchasing obligation limited to draught pils beer only, provided that the outlet purchased 50% or more of its total beer requirements from the brewer. This therefore limited the breadth and extent of the obligations imposed and allowed ABInBev's competitors to supply those tied outlets with any beers, except draught pils.³⁷⁵ Concessions were also made to allow these contracts to be terminated at any time on 3 months notice.³⁷⁶ Outlets operated under lease from Interbrew were subject to a reduced non-compete obligation that was limited to all types of draught beer brewed by ABInBev under its own brand or under a license agreement.³⁷⁷ Under the concessions granted, the tie no longer extended to draught beer that was not brewed by AB InBev.³⁷⁸ This subsequently opened up these outlets to competition from Trappist beers and others

³⁶⁸ Ibid at para 10, p14

³⁶⁹ Ibid at para 36, p16

³⁷⁰ Ibid at para 17, p15

³⁷¹ Above, n.366 at p58. See also J Ratliff, 'Major events and policy issues in EC competition law, 2002-2003: Part 2' (2004) 15 (3) I.C.C.L.R. 55 at p64 and 'European Commission: decision – beer supply sector-exclusive purchasing agreement exempted subject to access for competing beers', (2003) 24(9) E.C.L.Rev N153

³⁷² Above, n.364 at para 28, 16

³⁷³ Ibid at para 28, 16

³⁷⁴ Ibid at para 28, 16

³⁷⁵ Ibid at para 32,16. See also J Ratliff, 'Major events and policy issues in EC competition law, 2002-2003: Part 2' (2004) 15 (3) I.C.C.L.R. 55 at p64

³⁷⁶ Above, n.364 at para 33,16

³⁷⁷ Ibid at para 37,16

³⁷⁸ Ibid at para 37,16

not brewed by AB InBev.³⁷⁹ As Ratliff notes by agreeing to grant exemption to these agreements, the Commission appears to have taken into consideration the commercial interests of the supplier by negotiating these concessions as opposed to prohibiting the agreements as incompatible with Article 101 TFEU.³⁸⁰ However, while these concessions imposed more stringent requirements on AB InBev than were required under the terms of Regulation 2790/99 then in force, as noted in Chapter 3 it ultimately permitted AB InBev with a market share of 53% of the Belgian horeca sector to impose reasonably restrictive obligations on over half of Belgium's pubs.³⁸¹

4.3.2 Suspected cartel activity in the Belgian beer market

Notwithstanding the foregoing, excessive reliance on exclusive supply contracts is not the only practice of Belgium's largest brewers to attract the attention of the European competition authorities. In 2000, the European Commission investigated cartel activity in the Belgian brewing sector between Belgium's two largest brewers, AB InBev, then known as Interbrew, and Alken Maes a subsidiary company of Groupe Danone.³⁸² This was the first time the Commission had considered possible horizontal collusion between brewers.³⁸³ The alleged infringements included market sharing, price fixing and information exchange.³⁸⁴ In December 2001, the European Commission fined the two brewers, along with smaller brewers Haacht and Martens, for orchestrating two secret cartels on the Belgian beer market between 1993 and 1998.³⁸⁵ This decision was upheld on appeal.³⁸⁶

The first cartel involved the two largest suppliers of beer to the Belgian market, Interbrew and Alken Maes and concerned an extensive range of anticompetitive practices in both on and off-trade premises from 1993 until the beginning of 1998.³⁸⁷ Following increased

³⁷⁹ This was to be reviewed by the Commission should AB InBev opt to brew a Trappist or other such beer (ibid at para 39,16).

³⁸⁰ J Ratliff, 'Major events and policy issues in EC competition law, 2002-2003: Part 2', (2004) 15 (3)

I.C.C.L.R. 55 at p65

³⁸¹ Chapter 3 p95

³⁸² Press Release, 'The Commission fines brewers in market sharing and price fixing cartels on the Belgian market' (5th December, 2001) Brussels IP/01/1739

³⁸³ Ibid

³⁸⁴ Ibid

³⁸⁵ Commission Decision of 5 December 2001 in Case IV/37.614/F3 PO/ Interbrew and Alken-Maes ([2003] OJ L200/1) at para 329-330, 53 and para 342-344, 55

³⁸⁶ This was upheld on appeal to the General Court, Case T-38/02 Groupe Danone v. Commission [2005] ECR II-4407 and on further appeal, Case C-3/06P Groupe Danone v. Commission [2007] ECR I-1331. See also 'Competition: commission welcomes Court of Justice ruling in Danone case, confirming higher fines for repeat offenders' (8th February, 2007) Brussels MEMO 07/49

³⁸⁷ Their practices included concluding a general 'non-aggression pact', consulting on prices and promotions in the off-trade and customer sharing in the on-trade. Above, n.385 at para 1, 1 and para 281, 47. See also above, n.382 at p1.

threats from Danone to create difficulties for Interbrew on the French market, the brewers entered into a gentleman's agreement giving effect to these practices and subsequent 'cooperation' between the brewers.³⁸⁸ The Commission found this cartel, which covered all sectors of the market, to be a very serious infringement of Article 101 TFEU with this being reflected in the level of fine imposed which was intended to have a deterrent effect.³⁸⁹ The second cartel was concerned with private label beer. There had been consultation between the two largest brewers and brewers Haacht and Martens concerning this sector.³⁹⁰ The parties met and exchanged information regarding private label beer and Interbrew subsequently acknowledged that it was a party to an "*agreement on price level and market sharing in the private label market (1997-1998)*".³⁹¹ The Commission found that their practices were aimed at both sharing customers and at fixing prices above the level that would have been achieved under conditions of free of competition.³⁹² The brewers' cartel activities amounted to a concerted practice and a serious breach of Article 101 TFEU.³⁹³ The Commission did however take into consideration the shorter duration of the infringement, which lasted for 9 months,³⁹⁴ and the 'effective economic capacity' of the smaller brewers to cause significant damage to other operators in setting the level of the fines imposed.³⁹⁵ These were therefore not as significant as those for the first cartel however were intended to have a deterrent effect.³⁹⁶

4.4 The Belgian beer market today

In light of the foregoing it is clear that the practices of brewers in the Belgian beer market have not been entirely free of controversy, having attracted the attention of the European competition authorities for their widespread use of the beer tie as well as their concerted practices. However, notwithstanding this, and despite the market being significantly concentrated, as discussed above the Belgium brewing industry is still characterised by its great diversity. Persyn *et al* highlight that approximately 95% of Belgian brewers produce only 7% of Belgium's total beer production.³⁹⁷ Included amongst the products of these smaller brewers is Trappist beers the brewing and marketing of which remains within the

³⁸⁸ Above, n.385 at para 51, 8

³⁸⁹ Ibid at para 297-298, 49 and para 305, 50

³⁹⁰ Ibid at para 39, 6

³⁹¹ Ibid at para 156, 29 and para 161, 31

³⁹² Ibid at para 337, 54

³⁹³ Ibid at para 339, 54

³⁹⁴ Ibid at para 268, 48

³⁹⁵ Ibid at para 340, 54

³⁹⁶ Ibid at para 342-344, 55

³⁹⁷ Above, n.302 at p93

control of the Trappist monks.³⁹⁸ The authenticity of their products has been preserved by the imposition of strict rules governing their production that do not lend themselves to mass production by international brewers.³⁹⁹ The Belgian beer market is therefore characterised by a small number of very large breweries co-existing alongside a plethora of small brewers.⁴⁰⁰ This ‘dual market structure’ is similar to that existing in the UK beer market discussed in Chapter 4, and is also increasingly the case in the US and Australian markets due to their growing craft beer sectors.⁴⁰¹ The concentration now apparent in the Belgium beer market is therefore common to all of the beer markets considered here, and has been influenced by numerous factors beyond the acceptance or rejection of the beer tie as a legitimate business model.⁴⁰² As already mentioned, in Belgium the introduction of lager beer during the German occupation has been influential. However other generic factors that have contributed to this concentration in all beer markets include technological progress which has in turn lead to increased economies of scale, the development of powerful and nationally marketed beer brands, and declining beer consumption.⁴⁰³

4.4.1 Diversity distinguishes the Belgian beer market

Therefore whilst Belgium’s ‘dual market structure’ does not distinguish it from the UK beer market, the sheer number of beer varieties it supports does serve to do so. As already mentioned, on a *per capita* basis this is greater than any other country.⁴⁰⁴ As discussed above, a relaxed approach towards the beer tie has contributed to the maintenance of this diversity by providing a means for many smaller brewers to retain their market share in a rapidly consolidating industry. However, Persyn *et al* also suggest that the preservation of Belgium’s unique variety of beers is due to attempts by the larger brewers to maintain a portfolio of beers covering the most important traditional varieties.⁴⁰⁵ These brewers are active in the production of many different types of beer and endeavor to protect the image of regional quality products.⁴⁰⁶ The specificity of the production processes involved in

³⁹⁸ Ibid at p100

³⁹⁹ These rules also govern the labelling of products as an “Authentic Trappist product”. The International Trappist Association <<http://www.trappist.be/en/pages/trappist-beers>> accessed 20th March 2015

⁴⁰⁰ Above, n.302 at p93. See also See E Wauters and S Van Passel, ‘The more beers the better? Exploring the link between vertical integration in the brewery sector and beer diversity in pubs’ (Beeronomics, the Economics of Beer, Leuven, 28th May 2009) <http://www.beeronomics.org/papers/4B_Wauters.pdf> accessed 20th March 2015

⁴⁰¹ Above, n.302 at p93

⁴⁰² See E Wauters and S Van Passel, ‘The more beers the better? Exploring the link between vertical integration in the brewery sector and beer diversity in pubs’ at p1 (Beeronomics, the Economics of Beer, Leuven, 28th May 2009) <http://www.beeronomics.org/papers/4B_Wauters.pdf> accessed 20th March 2015

⁴⁰³ Above, n.302 at p94 and p96

⁴⁰⁴ Ibid at p79

⁴⁰⁵ Ibid at p92

⁴⁰⁶ Ibid at p93

producing some of these regional beers do not lend themselves to centralised production. It has therefore been suggested that the acquisition of some of these regional brands by a larger brewer has prevented them from disappearing from the Belgian beer market.⁴⁰⁷ Belgium's largest brewer AB InBev for example has an extensive portfolio of over two hundred brands and has a policy of retaining local beers in each country where it has a presence.⁴⁰⁸ It also has 'global flagship' brands that it promotes worldwide as 'premium brands' using the distribution networks for local brands to gain market share.⁴⁰⁹ However, the value in preserving this range of traditional Belgian beers is also influenced by the substantial and lucrative export market for them. As discussed above, Belgium is the second largest beer-exporting nation in Europe with international demand for Belgian beers continuing to increase.⁴¹⁰ Consequently all of these factors, in addition to Belgium's acceptance of the beer tie as a legitimate business model, have contributed to Belgium's significant diversity in terms of the beer varieties and producers operating in its beer market, at a time of declining global demand for beer.⁴¹¹

4.4.2 Increasing off-trade sales

In keeping with global trends in the beer industry already mentioned, the Belgium beer market is however declining.⁴¹² Whilst as discussed above, international demand for Belgian beers has long compensated for declining domestic consumption, another implication of this has been the recent shift away from on-trade beer sales through Belgium's horeca sector of the market. Belgian brewers, like many of their European counterparts, have responded by increasing the support offered to the hospitality sector. However Belgian brewers have also placed significant effort in developing novel beers as consumers have favoured local premium brands over mainstream lagers due to a trend of pairing specialty beers with cooking.⁴¹³ Whilst the on-trade sector remains strong, in 2009 off-trade consumption was greater than on-trade beer sales for the first time in several

⁴⁰⁷ Ibid at p93

⁴⁰⁸ Ibid at p99-100. Also Datamonitor, 'Global Brewers 2011' at p23

⁴⁰⁹ Its global flagship brands include Becks, Budweiser and Stella Artois. Datamonitor, 'Global Brewers 2011' at p23. Also, n.302 at p99-100

⁴¹⁰ B Berkhaut et al, 'The contribution made by beer to the European Economy' at p74 (*Ernst & Young*, 2013) and M Brink et al, 'The contribution made by beer to the European Economy', *Ernst & Young* (Amsterdam, 2011) at p60. See also n.302 at p103

⁴¹¹ Above, n.302 at p103

⁴¹² The Belgian beer market shrank by 1% in 2013. See above, n.342 at p8. For over 30 years Belgians have also been drinking less beer. Above, n.302 at p80

⁴¹³ B Berkhaut B et al, 'The contribution made by beer to the European Economy' at p75 (*Ernst & Young*, 2013) <[http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/\\$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf](http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf)> accessed 2nd July 2015

years with this trend continuing today.⁴¹⁴ As discussed above, a similar trend is evident in the UK beer market, and has also long been evident in the US and Australian beer markets in light of their outlawing of the beer tie. In 2013, supermarkets accounted for 46.5% of the Belgian beer market distribution by value, with the on-trade accounting for 32.5% of the market.⁴¹⁵ The largest off-trade channel in the Belgian beer market is therefore the supermarket. As is also evident in the UK and Australian beer markets, the Belgian supermarkets enjoy significant buyer power and so are able to negotiate preferred terms on price with brewers with the supermarkets' low switching costs and their increasing production of private labels contributing to this buyer power.⁴¹⁶

As mentioned above, the Belgian on-trade sector is still strong and the chain of distribution in the Belgian beer market involves the on-trade sector being supplied by beer wholesalers.⁴¹⁷ Whilst consolidation within the wholesale sector has caused a decrease in the number of such wholesalers in operation it is still considered to be reasonably large.⁴¹⁸ As already mentioned concerns over the distribution of beer in the UK have included the absence of an independent wholesale and distribution sector. Some Belgian wholesalers specialise in supplying the on-trade whilst brewers also distribute directly to the trade.⁴¹⁹ However in addition to tying outlets within the horeca sector, Belgian brewers have been known to acquire these beer merchants as the largest of these often own pubs.⁴²⁰

Consequently despite having a competition law regime that is very similar to that in the UK and recognises the beer tie as a legitimate business model, the Belgium beer market has no equivalent to the UK's pubcos in the supply chain of beer distribution. The closest to this would be those Belgian beer wholesalers who also own pubs, however, no competition law issues appear to have been raised regarding their practices. This a very different proposition from the UK's pubcos, which were ultimately an unforeseen consequence of the Beer Orders of 1989 as discussed in Chapter 2.

⁴¹⁴ Ibid at p74

⁴¹⁵ Specialist retailers accounted for 17.1%, convenience stores 1.6% and others made up the remaining 2.4%. Above, n.342 at p13.

⁴¹⁶ Ibid at p17 and above, n.385 at para 8, 2

⁴¹⁷ Above, n.385 at para 7, 2

⁴¹⁸ Ibid at para 7, 2

⁴¹⁹ Ibid at para 7, 2

⁴²⁰ Above, n.402 at p4

4.5 Belgian approach to beer distribution preferable to that in the US and Australian markets

In light of the foregoing it is evident that there are some similarities between the Belgian beer market and the UK market. Both share a ‘dual market structure’, which is also increasingly evident in the US and Australian markets. Whilst both are significantly concentrated, as is a trend in the global brewing market, the levels of concentration amongst the largest producers in Belgium and the UK are less than those in the US and Australian markets. The Belgian beer market is however distinguishable from the other beer markets considered here on account of its trademark diversity. This has been retained under a legal regime that is very similar to that in the UK under the Competition Act 1998 discussed in Chapter 4. Modeled on the EU competition law provisions both recognise the beer tie as a legitimate business model for the distribution of beer.

Whilst Belgium’s legal regime has contributed to the maintenance of its diversity, acceptance of the beer tie alone does not account for the extensive range of Belgian beer products and producers operating in the market today. As discussed above, Belgium’s geographical position in Europe and the historical influences on the range of brewing techniques utilised in the country have played a significant role in this. The largest Belgian brewers’ desire to maintain an extensive range of brands that utilise traditional brewing techniques, and the increasing international export market for Belgian beers have also been influential. As has the recent trend in favour of consuming local premium brands over mainstream lagers.

However, notwithstanding the diversity in the Belgian beer market, the competitive implications arising from the extensive use of the beer tie by the country’s largest brewers have also attracted the attention of the European competition authorities as exemplified in *Interbrew*. This serves as a reminder of the potential competitive implications arising from the widespread use of such vertical restraints which as discussed in Chapter 4 has long been a feature of the UK beer market. Consequently, whilst it is undoubtedly the case that acceptance of the beer tie as a legitimate business model requires its use by the largest market participants to be closely monitored by the competition authorities given its potential to, amongst others aid market foreclosure, the Belgian beer market serves to highlight that recognising the tie as a legitimate business model is not in itself objectionable. In light of the foregoing consideration of the Belgian beer market, acceptance of the beer tie as a legitimate business model is preferable to the approaches adopted in the USA and Australia. However, in light of the peculiarities of the UK market,

most notably the existence of the pubco, and in order to address the on-going concerns discussed in Chapter 4 over its use which ultimately prompted the adoption of the 2015 Act, in the context of the UK while outlawing the tie as an illegitimate business model may not be desirable, the beer tie requires to be rebalanced.

5. Conclusion

The foregoing review of beer distribution in the selected geographic markets highlights that there are several factors influencing the current structure of these markets. This includes the approach adopted towards vertical integration and the acceptance of beer tying agreements. As discussed above there are limits to the weight that can be afforded to international comparisons, however consideration of these geographic markets suggests a broad trend between outlawing the tie and considerable consolidation following. This is notwithstanding the fact that consolidation has been a feature of all of the markets considered given the influence of, amongst others, declining global beer consumption and the need for brewers to maintain economies of scale to ensure economic production.

Consideration of the US beer market has shown that outlawing the beer tie as a legitimate business model and imposing a mandatory separation between each tier in the distribution chain does not produce a very competitive system for the distribution of beer. Efficiency was not however the goal of the US authorities at the time of implementation of the 3-tier system, with public policy considerations being the driving force behind its adoption. Nevertheless, as has been shown above, this has facilitated the creation of a duopolistic market structure today. Further, some relaxation of the prohibition on vertical integration by brewers through very narrow exceptions to the 3-tier system has been necessary to facilitate the development of a craft beer sector to challenge the market power of the largest brewers. Consequently acceptance of some vertical integration in the market has been required in order to increase consumer choice beyond the duopolists' products. The 3-tier system has also been shown not to present a solution to the UK market's lack of an independent wholesale and distribution sector. Despite distributors being placed at the centre of the 3-tier system and being afforded Federal and State protection, due to factors including their alignment with the dupolists, the 3-tier system has not established an entirely 'independent' wholesale and distribution sector. The foregoing review of the US beer market therefore suggests that merely outlawing the tie as an illegitimate business model and imposing a mandatory layer of distributors is not a model that is suitable to be followed in reforming the distribution of beer in the UK.

Australia however has not gone as far as the US in terms of deeming the tie an illegitimate business model in all circumstances. It has nevertheless adopted a stricter approach than the UK. While Australian markets are generally relatively small and concentrated, following the introduction of s.47 TPA and the Tribunal's decision in *Tooth*, the market has evolved into a duopoly, with the two largest brewers having a combined market share exceeding that of the US duopolists. This has ultimately impacted on consumer choice with a recent resurgence in the craft beer sector being prompted by Australian consumers' demands for greater choice beyond the duopolists' products. The resulting increase in the craft sector's market share has been facilitated without amendment to the legal regime, as was necessary in the US, given Australia's acceptance of the beer tie and vertical integration in certain circumstances. However, as in the UK beer market, this increased diversity is not reflected in the Australian on-trade due to the continued use of beer tying agreements by Australia's largest brewers, with this reportedly prompting investigation by the ACCC. This serves to highlight the consequences of the use of the beer tie by the country's largest brewers, however given the implications of an absolute prohibition on exclusive dealing as in the US market, including restricting the development of a brewing sector to challenge the largest players, the Australian market highlights that some acceptance of exclusive dealing is preferable to outlawing this entirely.

A further implication of Australia's stricter approach to exclusive dealing is that off-trade beer sales have long exceeded those through the on-trade. While this is an increasing global trend affecting all of the beer markets considered, this was expedited in Australia, as it was in the US, due to the general prohibition on exclusive dealing and the decision in *Tooth*. Although supermarkets undoubtedly offer low cost options for consumers, their development of private labels and significant bargaining power also have implications for the beer market going forward with their practices attracting the attention of the ACCC. This is therefore a potential implication of reform that should inform proposals for the UK market.

Consequently, the Australian approach highlights that some acceptance of vertical integration is preferable to outlawing this entirely. However Australia's stricter approach to the beer tie has generally resulted in significant concentration in the market and there are similarities in the on-going competitive issues raised in the UK and Australian beer markets today. The Australian approach therefore does not appear to present a suitable model to be followed in reforming the distribution of beer in the UK.

The advantages of accepting the beer tie as a legitimate business model are also supported by the foregoing review of the Belgian beer market. Whilst the Belgian beer market has undergone significant consolidation in line with the on-going global trend, this has not been as great as that in the US or Australian markets. Today the Belgian market similarly to the UK market has a ‘dual market structure’ under which it has retained its trademark diversity. This has developed under a legal regime, almost identical to the UK’s, which is modelled on the EU competition law provisions and so recognises the tie as a legitimate business model. Other factors beyond acceptance of the beer tie have however been acknowledged as contributing to this diversity, including the desire of the largest brewers to maintain broad portfolios of brands utilising traditional techniques and the extensive export market for Belgian beers.

However, notwithstanding this diversity the competitive implications of the largest brewers placing reliance on the beer tie have also affected the Belgian market. This was illustrated by the European Commission’s involvement in *Interbrew*. This highlights the potential competitive implications associated with the widespread use of such vertical restraints which, as discussed in Chapter 4, is an on-going issue in the UK beer market. Therefore whilst it is clear that acceptance of the beer tie as a legitimate business model requires its use, especially by the largest market participants, to be closely monitored by the competition authorities due to the dangers of amongst others market foreclosure, consideration of the Belgian beer market highlights that accepting the tie as a legitimate beer model is not in itself objectionable from a competitive perspective.

From the foregoing review of these selected geographical markets it is subsequently suggested that UK and Belgian approach of accepting the beer tie as a legitimate business model is preferable to those adopted in the USA and Australia. However, in light of the peculiarities of the UK beer market, particularly the existence of the pubco, and the numerous and on-going concerns surrounding their operation of the beer tie, it is suggested that while the beer tie should not be prohibited outright in the context of the UK market, it requires to be rebalanced. In light of this it is instructive in the next chapter to consider whether another market in the UK that shares some of the characteristics of the beer market and also relies heavily on tying agreements, namely the petroleum market, has also faced the same issues as the brewing industry.

Chapter 6 - A Comparison of Beer and Petroleum Distribution in the United Kingdom

The preceding chapter considered, by way of comparison, the lessons that may be learned from selected non-UK markets when making recommendations for the future reform of the distribution of beer in the UK. It was suggested that in light of the experience in the US and Australian markets, following the outlawing of the beer tie as a legitimate business model, that rebalancing not outlawing the beer tie is the preferred option for the reform of the distribution of beer in the UK. This chapter now considers whether another market in the UK that shares several characteristics of the beer market and also relies heavily on tying agreements, namely the petroleum market, has also faced the same issues as the brewing industry in order to further guide proposed reforms of the distribution of beer in the UK.

The chapter first notes the similarities in the distribution of beer and petrol highlighting their vertically integrated distribution systems, their reliance on vertical restraints and increasing buyer power in both markets (Subsection 1). It then focuses on the special handling of both of these sectors at the EU level noting the provisions of the various Block Exemption Regulations and touching on the decisional practice of the European Courts and Commission (Subsection 2). The chapter then highlights the numerous and on-going competition concerns that have affected both markets including early concerns over vertical integration and possible monopoly situations (Subsection 3). Regard is had to structural changes and the Office of Fair Trading's (OFT) declarations of competitiveness in the beer and petroleum markets (Subsection 4). The chapter then turns to consider the on-going challenges facing both sectors (Subsection 5). Continued discontentment over the operation of these markets is also considered noting the newly adopted Small Business, Enterprise and Employment Act 2015 (2015 Act) with regard to the beer market and the OFT Call for Information on the UK petrol and diesel sector in 2013 (Subsection 6). The chapter then highlights the continued lack of anticompetitive declarations in both sectors (Subsection 7). It then considers the distinguishing features in the supply of beer and petrol (Subsection 8). Finally the rise and influence of supermarkets in the distribution of beer is addressed (Subsection 9).

1. Similarities in the distribution of beer and petrol

As already discussed in Chapter 3, there are many similarities between the distribution of beer and petrol. As noted by Goyder, both industries involve ‘liquid products which are consumed or utilised on a regular basis in small quantities by individual consumers and have to be provided from a large number of outlets across a wide geographical basis.’¹ They are also similar in that both are scale economy industries and as such brewers and refiners have long strived to utilise the full capacity of their facilities in an attempt to keep their costs at an acceptable level. Consequently, producers in both have sought control of guaranteed retail outlets for their products and have gone about this in similar fashions.² As a result, and as discussed in Chapter 3, within both industries there is a natural tendency towards vertical integration with the widespread ownership of retail outlets and the use of exclusive purchasing agreements being employed in the distribution of beer and petrol in order to achieve this.³

1.1 Vertically integrated distribution systems

1.1.1 Retail distribution of beer

As discussed in Chapter 2, a high level of vertical integration has been achieved in the retail distribution of beer through the practice of tying retail outlets, with very similar mechanisms also being employed in the retailing of petrol. As discussed earlier, initially breweries owned public houses and other retail outlets, and only permitted the sale of their product from these premises.⁴ They also influenced the ‘free-trade’ in independently owned public houses by securing exclusivity for their products in exchange for loans on favourable terms.⁵ Whilst these practices ultimately prompted the Beer Orders in 1989, marking the demise of the large tied estates of the national brewers, today the majority of public houses in the UK are still tied to the supply of beer from a small number of large international brewers. However, as discussed in Chapter 2, following the Beer Orders this supply is now largely facilitated by pub companies (pubcos).⁶ Whilst operating independently of the brewing industry, they have perpetuated the tied house system by owning significant estates of public houses supplied by a single brewer, most often one of the largest brewers with the strongest brands and the greatest discounts on wholesale beer

¹ D.G. Goyder, *EC Competition Law* 3rd Edition (Oxford, Oxford University Press, 1998) at p203

² The Monopolies Commission, *Petrol, A Report on the Supply of Petrol to Retailers in the United Kingdom* (Cmnd 264, 1965) at para 58, p20

³ Chapter 3, p57

⁴ See Chapter 2.

⁵ This practice developed early on. See Chapter 2, p13

⁶ Chapter 2, p40

prices. Consequently, economies of scale are maintained under the pubco's tie. However, as discussed in Chapter 4, another aspect of the pre-Beer Orders market that is still evident today is that whilst some pubcos have their own distribution networks, many outsource distribution to the largest brewers which today are international organisations.⁷ As a result, there is still no strong independent wholesale sector in the distribution of beer in the UK as the largest brewers still dominate the market with their distribution systems and discounts.

1.1.2 Ownership of public houses

However, whilst as discussed in Chapter 4, pubcos have come to have significant tied estates, no pubco holds a dominant position under the UK or EU competition law provisions.⁸ Nevertheless, a high level of vertical integration still exists in the market today. The different models of ownership of public houses can be broken down into three broad categories, namely pubco owned outlets; brewer owned outlets; and independently owned or 'freehold' outlets.⁹ As discussed in Chapter 2, the tied sector comprising brewer owned and pubco owned outlets, can be further subdivided into 'tenanted or leased' outlets and 'managed' outlets. Under the 'tenanted or leased' model, the brewer owns the public house however a tenanted landlord runs the business independently and pays rent in return, with the business being tied to the brewer's or pubco's products.¹⁰ Under the managed model, the owning brewer or pubco employs a manager who is an employee of the company and runs the public houses on behalf of the owning pubco or brewery.¹¹ No rent is payable under the managed model. The overall effect of these different models of ownership and management is to ensure a high degree of vertical integration in the distribution system and the maintenance of economies of scale, with close parallels being evident in the techniques employed in the retail distribution of petrol.

1.1.3 Retail distribution of petrol

Significant similarities are apparent in the retail distribution of beer and petrol on account of the high levels of vertical integration within these markets, and the means employed to achieve this. This is so, even although some structural changes within the petrol industry have reduced this from its peak levels during the 1960-1970s, when the industry was characterised by substantial vertically integrated supply chains dominated by the major

⁷ Chapter 4, p118

⁸ Chapter 4, p118

⁹ Chapter 2, p31

¹⁰ As discussed in Chapter 2, tenanted public houses are a remnant of the old brewery tied house system, with leased houses being a modern version.

¹¹ R Hucker, (ed) 'Market Report 2013, Public Houses' (Key Note, 2013) at p4

international oil companies.¹² Consequently, as in the brewing industry there has been some supply chain fragmentation although in the petrol industry this has been influenced by cost savings and the desire to increase efficiency, not Government intervention as in the brewing industry.¹³ Despite this, oil majors such as BP, Esso and Shell, still operate as both refiners and wholesalers of petrol and also own their own forecourts.¹⁴ Therefore, as with the large international brewers in the brewing industry, the large international oil companies have retained an important role in the distribution of petrol. However, in contrast to the brewing industry where distribution is still largely dominated by the largest brewers, within the petrol industry, whilst in the 1970s-1980s the wholesalers who supplied petrol stations with fuel were primarily those with refining capacity, they also included independent wholesalers who lacked refining capacity.¹⁵ These independent wholesalers varied considerably in size and obtained fuel supplies from UK refiners under individual contractual terms.¹⁶ Today, the wholesale market is made up of a range of undertakings utilising different business models. The most predominant of these are UK refiners who sell directly to retailers; wholesalers who either import fuel from overseas or obtain it from UK refineries and sell it to retailers and other wholesalers; blenders who purchase fuel components and complete the production process themselves; and oil companies which are ultimately the wholesaler for their own product.¹⁷ Subsequently, this is more differentiated than the wholesale sector in brewing which is largely dominated by the largest brewers and pubcos.

1.1.4 Ownership of petrol stations

Similarly to the ownership of public houses, the ownership of petrol stations can be broken down into three broad categories. These are the traditional petrol retailing oil company-owned sites; independent dealers that are not part of an oil company but are also considered to be a traditional petrol retailer; and the newer but increasingly significant

¹² Deloitte, 'Study of the UK petroleum retail market A Final Report for DECC' (December 2012) *UK Government*, 2012) https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/69760/7322-study-of-the-uk-petroleum-retail-market.pdf accessed 14th October 2014. Those that owned refineries often supplied branded petrol stations that were generally owned by the supplying company or were independently held and branded by the supplying oil major (ibid at p17-18). This changed after the oil shock in 1970, when crude oil prices fell and stayed low until 2000. As these organisations looked for cost savings, in the 1980s they cut their own distribution channels and developed exchanges and partnerships with other oil companies (ibid at p18)

¹³ Ibid at p6

¹⁴ The Monopolies and Mergers Commission, *The Supply of Petrol a Report on the supply in the United Kingdom of petrol by wholesale* (Cm 972, 1990) at para 3.24, p19

¹⁵ Ibid at para 3.51, p30

¹⁶ Ibid at para 3.45, p29

¹⁷ Office of Fair Trading, *UK petrol and diesel sector An OFT Call for Information* (OFT 1475, 2013) at para 3.31, p39-40

supermarket owned sites.¹⁸ As is the case in the ownership of public houses, no company has been found to hold a dominant position under the UK or EU competition law provisions. Nevertheless, as with public houses a significant level of vertical integration has been achieved through these different models of ownership and the management of these sites similarly to tied pubs. Oil company owned sites can be operated along the lines of a ‘managed’ public house, and as such operated by the oil company’s own retail subsidiary,¹⁹ or they may also be licensed or leased to another individual or group, similarly to a ‘tenanted or leased’ public house, tied to its products.²⁰ However, recently the structure of the market has been altered by the significant growth in supermarket forecourts. In the late 1980s, there was an increase in supermarkets selling fuel in order to attract customers to their stores by making offers on fuel.²¹ Today, this model increasingly dominates the market due to the significant cost savings they offer consumers through low retail prices.²² Supermarkets’ share of the retail fuel market has been rising at such a consistently strong rate that they have significantly challenged the traditional petrol retailers, whose share of the market has been declining.²³ However, despite this growth, the largest proportion of petrol stations in the UK are owned by independent dealers and so are held and operated by an individual or group which is not part of an oil company or a supermarket.²⁴ Nevertheless, only a very small proportion of these independent sites are unbranded with most of them retailing fuel under the brand name and sign of the supplying oil company to which they are tied.²⁵ Similarly to tied publicans, retailers enter into solus agreements that impose exclusive purchasing obligations on them, which are very similar to those imposed on tied public houses under beer tie agreements. Consequently, the market is still highly integrated and exhibits significant similarities to the distribution of beer.

1.2 The solus tie – the beer tie’s equivalent

As in the brewing industry, vertical restraints have been widely used to replicate the effects of vertical integration and so have played an important role in the retailing of petrol. The most common form of vertical restraint in the distribution of petrol, as is the case with beer, is the imposition of exclusive purchasing obligations on retailers with solus

¹⁸ Above, n.12 at p28

¹⁹ Ibid at p28

²⁰ Ibid at p28

²¹ Ibid at p18

²² Ibid at p18. The major supermarkets include Tesco, Asda, Morrisons and Sainsbury’s.

²³ Ibid at p29

²⁴ Where a supermarket retails fuel under the brand of an oil company and not under their own brand name, they are regarded as independent dealer-owned sites (ibid at p28-29).

²⁵ Ibid at p28

agreements being the equivalent of the beer tie in the brewing industry. These agreements were introduced into the UK by the large international oil groups which used them abroad and effectively tie the petrol station in question to a single petrol wholesaler.²⁶ Their use was justified on the basis of the significant capital investment in refineries that required “careful consideration...be given to economies in distribution methods, to ensure that a reasonable return would be obtained from such capital investment.”²⁷ Consequently, similarly to the beer tie, solus agreements essentially require independent branded dealers agreeing to a branded wholesaler being the sole supplier of motor fuel to its site.²⁸ The solus agreement is however only one type of supply agreement, with the characteristics of the contractual relationship between the wholesaler and retailer varying with the type of forecourt in question.²⁹ Consequently, unbranded sites can source fuel from different fuel suppliers. Similarly, given that supermarkets often sell fuel under their own brand name, and not that of an oil company, they may have a contract with a single wholesaler for the supply of all of their sites, or they may have numerous supply agreements in place.³⁰ Given their size and influence, their terms of supply are generally preferable to those offered to solus tied forecourts, due to the fact that as, is now the case with the pubco in the distribution of beer, supermarkets also enjoy increased buyer power.³¹ This development has however had implications for both industries.

1.3 Increased buyer power in beer and petrol industries

The changes that have occurred in both markets through the growth of the pubco in the retail distribution of beer, and the supermarket forecourt in the retail distribution of petrol, include the fact that both enjoy countervailing buyer power in relation to the major brewers and petrol wholesalers in their respective industries.³² As discussed in Chapter 2, the countervailing buyer power now enjoyed by pubcos has brought about a reduction in the average net wholesale price of beer.³³ Similarly, supermarket forecourts due to the volume of sales they account for, coupled with their ability to draw on a wide range of suppliers, have been able to negotiate lower wholesale petrol prices compared to other independent retailers.³⁴ While, as discussed in Chapter 2, these reductions have not filtered through to the average retail price of beer in the pubco controlled on-trade, in the petrol industry these

²⁶ Above, n.2 at para 58, p20

²⁷ Ibid at para 58, p20, quoting oil company Anglo-American

²⁸ Above, n.14 at para 3.59, p33

²⁹ Above, n.12 at p47

³⁰ Ibid at Table 6, p48

³¹ Ibid at Table 6, p48

³² Above, n.17 at para 5.4, p88-89

³³ Chapter 2 at p44

³⁴ Above, n.17 at para 5.4, p88-89

reductions have filtered down into lower pump prices at supermarket forecourts.³⁵ Nevertheless, a consequence of this countervailing buyer power in both sectors and its respective effect on retail prices has ultimately been the closure of public houses and forecourts. The failure of pubcos to pass on discounts in wholesale prices to their tied lessees has increased retail prices and undermined the viability of tied public houses which have continued to close.³⁶ Similarly, as will be discussed more fully below, the low pump prices charged by supermarkets and the ensuing aggressive competition between oil company and supermarket owned sites has caused extreme squeezing of retail margins and ultimately accelerated the closure of independent forecourts. The overall effect in both sectors has been a continued decline in the number of public houses and petrol forecourts in operation.³⁷ Nevertheless, due to the many similar, and largely unique, features shared by these markets, beyond the countervailing buyer power now common to both, they have been singled out by the EU competition authorities as deserving of special treatment under the EU competition law provisions.

2. Special handling for both sectors at the EU level

As discussed in Chapter 3, the many similarities between the retail distribution of beer and petrol have been deemed sufficient by the EU to merit the special treatment of exclusive purchasing agreements within these industries under the EU competition law provisions. This is a largely unique approach that contrasts with the American and Australian competition law regimes considered in Chapter 5, which do not make special provision for such agreements in the brewing industry, except in so far as they are outlawed. Whilst the EU's position has been influenced by several factors including integration as a unique, but overarching, goal of the EU competition law regime, this special deference towards EU beer tie and service station or solus agreements³⁸ has contrasted not only with the treatment of similar agreements in other jurisdictions, considered in Chapter 5, but also with the treatment of similar arrangements in other sectors of the economy.

2.1 The EU block exemption regulations

The EU's largely unique approach to the beer tie and service station agreements has been influenced by several factors. As discussed in Chapter 3, the beer and petrol industries have long enjoyed special handling at the EU level on account of the significant capital

³⁵ Above, n.12 at p10

³⁶ Chapter 4, p 127

³⁷ Above, n.12 at p2.

³⁸ The term 'Solus agreement' is used interchangeably in this chapter with the term 'service station agreement' as referred to in the context of the European Block Exemption regulations.

investment suppliers have had to make in the retail outlets for their products.³⁹ This was most evident in the terms of Regulation 1984/83.⁴⁰ Due to the large capital outlays involved in acquiring such an outlet, breweries and oil companies frequently bought and leased premises to resellers or almost always financed the acquisition of sites as well as offering loans on favourable terms. The EU placed reliance on such ‘peculiarities of the markets in question’⁴¹ in order to justify its approach. General concerns over the foreclosure effects of the widespread use of such agreements were overlooked due to the ‘special commercial or financial advantage’ conferred on the resellers under the exclusive purchasing agreements in these sectors.⁴² As discussed in Chapter 3, the European Commission considered this made it significantly easier for resellers to establish, operate and maintain premises and were therefore credited with aiding integration, efficiency and low cost entry to both industries with consumers enjoying a fair share of the resulting benefits.⁴³

2.1.1 Position pre-Regulation 1984/83

The first Block Exemption Regulation (BER) was not adopted until 1967.⁴⁴ Prior to this, the assessment of the legality of service station agreements, like that for beer supply agreements, was in accordance with the decisional practice of the European Commission and Courts discussed in Chapter 3.⁴⁵ Although there were no express rules in Regulation 67/67⁴⁶ regarding beer or service stations agreements, by including exclusive purchasing agreements they were implicitly included. Sector specific rules first appeared in Regulation 1984/83. The provisions applicable to beer supply agreements were noted in Title II, discussed in Chapter 3, and those relevant to service station agreements were in Title III. There were significant similarities between them.

2.1.2 Title III of Regulation 1984/83 - special provisions for service station agreements

In light of the similar justifications provided for the exemption of beer and petrol supply agreements, it was unsurprising that the terms of Title III of Regulation 1984/83 reflected

³⁹ See Chapter 3, p66

⁴⁰ Commission Regulation (EEC) 1984/83 of 22 June 1983 on the application of Article 85(3) of the Treaty to categories of exclusive purchasing agreements ((1983) OJ L173/5)

⁴¹ See Chapter 3, p66

⁴² See Chapter 3, p67

⁴³ See Chapter 3, p67

⁴⁴ See Chapter 3, p60

⁴⁵ See Chapter 3, p57

⁴⁶ Commission Regulation (EEC) No 67/67 of 22 March 1976 on the application of Article 85(3) of the Treaty to certain categories of exclusive dealing agreements ((1967) OJ (spec ed) 10)

those of Title II.⁴⁷ The provisions of Article 10 regarding petrol station agreements were therefore very close to those of Article 6(1) regarding beer. It stated that an exemption would be granted to ‘agreements where only two undertakings are party and the reseller agrees with the supplier, in consideration for the according of special commercial or financial advantages, to purchase only from the supplier, or an undertaking connected or trusted by the supplier with the distribution of his goods, certain petroleum-based motor-vehicle fuels or certain petroleum based motor vehicle and other fuels specified in the agreement for resale in a service station designated in the agreement’.⁴⁸ Consequently, the exemption applied to agreements concerning motor vehicle fuels alone, such as diesel or petrol, or these and other fuels, such as paraffin.⁴⁹ The Commission clarified that the goods in question had to be petroleum-based products and they had to be for use in motor powered land or water vehicles or aircraft, with “*service station*” being interpreted accordingly.⁵⁰ However, the reference to ‘resale’ prevented the Regulation applying to services.⁵¹ Consequently, the provisions for petrol were very close to those for beer.

2.1.2.1 The ‘white’ list for service station agreements

Article 11 of Regulation 1984/83 however detailed a simpler, exhaustive ‘white’ list of obligations that the supplier could impose on the reseller in service station agreements by comparison to those for beer supply agreements.⁵² Article 13 also incorporated the terms of Article 2(1) and (3) of Title I regarding exclusive purchasing agreements in all sectors of the economy, into Title III.⁵³ Following on from the provisions relating to beer supply agreements under Title II, Article 11(a) allowed the imposition on the reseller of the obligation not to sell motor vehicle fuel and other fuels supplied by other undertakings, in the designated service station. However, in contrast to the white list for beer, Article 11 was not restricted to petroleum-based fuels or fuels of the same type as those sold under the agreement in the designated premises, suggesting that the possibilities for tying under this Title were not as narrow as those for beer.⁵⁴ Article 11(b) also differed from the white list for beer by permitting a limited tie of lubricants or related petroleum-based products,

⁴⁷ Chapter 3, p 67

⁴⁸ Article 10, Title III of Regulation 1984/83

⁴⁹ European Commission, *Notice concerning Commission Regulations (EEC) No 1983/83 and (EEC) No 1984/83 of 22 June 1983 on the application of Article 85(3) of the Treaty to categories of exclusive distribution and exclusive purchasing agreements* ((1984) OJ C 101/2) at para 58, p9

⁵⁰ Ibid at paras 58-59, p9. V Korah and W.A. Rothnie W.A., *Exclusive Distribution and the EEC Competition Rules Regulations 1983/83 and 1984/83* 2nd Edition (London, Sweet and Maxwell, 1982) at para 8.23, p233

⁵¹ V Korah and W. A. Rothnie, *Exclusive Distribution and the EEC Competition Rules Regulations 1983/83 and 1984/83* 2nd Edition (London, Sweet and Maxwell, 1982) at para 8.23, p233

⁵² Chapter 3, p68

⁵³ Chapter 3, p65-66

⁵⁴ Above, n.51 at para 8.24, p234

such as brake fluids.⁵⁵ The supplier could impose an obligation ‘not to use lubricants or related petroleum based-products supplied by other undertakings within the service station, where it had made available or financed a lubrication bay or motor vehicle lubrication equipment’. However the Commission clarified that this provision was concerned more with the use of these products, and so the provision of a service, rather than the reseller’s freedom to purchase the products from undertakings for resale in the service station.⁵⁶ In keeping with the provisions of Title II, minor restrictions could be imposed in respect of advertising goods supplied by other undertakings.⁵⁷ However, Article 11(d), which was unparalleled in Title II, permitted an obligation to have equipment owned or financed by the supplier, or a connected undertaking, serviced by the supplier. Korah and Rothnie note that this was a justifiable imposition on the reseller as such equipment would not be provided if the supplier could not ensure proper maintenance.⁵⁸ Subsequently, by contrast to Title II, as the provisions regarding service station agreements did not limit exemption to specified products, and due to the smaller range of products supplied by oil companies, the wording of the petrol ‘white’ list was simpler than that for beer.⁵⁹

2.1.2.2 The ‘black’ list for service station agreements

Similarly to Article 8 of Title II regarding beer supply agreements,⁶⁰ Title III also adopted a ‘black’ list approach to restraints, the inclusion of which would deny an agreement the benefit of exemption. Article 12(1)(a) precluded the supplier from imposing exclusive purchasing obligations for goods other than motor vehicle and other fuels or for services. The exceptions to this were obligations under Article 11(b) not to sell lubricants or petroleum related products supplied by other undertakings in that service station; and the obligation to have equipment owned or financed by the supplier serviced by them, under Article 11(d). This effectively limited the exclusive purchasing obligation to the fuels, lubricating oil, and servicing equipment provided by the supplier and exempted under Articles 10 or 11.⁶¹ This was reinforced by Article 12(1)(b), which denied exemption where the reseller was prevented from obtaining goods or services from third parties where

⁵⁵ Above, n.49 at para 61, p9 and above, n.51 at para 8.24, p235

⁵⁶ Above, n.49 at para 61, p9

⁵⁷ Article 11(c) Regulation 1984/83

⁵⁸ Above, n.51 at para 8.24, p236

⁵⁹ Ibid at para 8.25, p237-238

⁶⁰ Chapter 3, p69

⁶¹ Above, n.51 at para 8.25, p237

neither an exclusive purchasing obligation nor a ban on dealing with competing products was allowed.⁶²

Concerns over foreclosure influenced the terms of Article 12 (1)(c), which limited the duration of service station agreements to ten years and denied exemption to those of a longer or indefinite duration. However, in keeping with the position regarding beer, this was twice as long a duration as permitted under Title I regarding exclusive purchasing agreements in all sectors of the economy. In line with Title II however, Article 12(1)(d) limited the obligations that could be imposed on successors in title. Nevertheless, concerns regarding exclusive purchasing obligations of long durations, resulting in time limits for such restraints in all other sectors, seemed to be disregarded under by the terms of Article 12(2). As with tied public houses leased to the reseller, Article 12(2) stated that where the supplier lets or allows the reseller to occupy the service station, the exclusive purchasing obligation could be imposed on the reseller for the duration that they operate from the premises. However, in contrast to the provisions of Title II, there was no obligation to include an ‘English Clause’ in such circumstances.⁶³ Unlike the provisions for beer, allowance was made in the Regulation for national authorities to impose a shorter duration limit on such agreements than that prescribed under Article 12.⁶⁴ Further, even although the terms of Title III were prescriptive, petrol companies were noted to be ‘reasonably happy’ with its application in regard to the supply of petrol to garages.⁶⁵

2.1.3 The CJEU’s approach to parallel networks of service station agreements

In addition to the foregoing similarities under Regulation 1984/83, parallels were also apparent in the Court of Justice of the European Union’s (CJEU) handling of beer supply agreements discussed in Chapter 3 and service station agreements as evidenced in its decision in *Neste*.⁶⁶ There the CJEU also sought to limit the application of Article 101(1) TFEU to such agreements. *Neste* arose from a preliminary reference connected with an exclusive purchasing obligation for petrol and other products sold in Finnish service

⁶² Ibid at para 8.25, p237

⁶³ See Chapter 3, p71

⁶⁴ National laws and measures imposing a shorter duration limit were not incompatible with the objectives of the Regulation which set an upper duration limit on service station agreements (Recital 19, Regulation 1984/83)

⁶⁵ Above, n.51 at para 11.12, p295

⁶⁶ (Case C-214/99) *Neste Markkinointi OY v. Yötuuli KY* [2001] 4 CMLR 993

stations.⁶⁷ The parties had entered into a ‘co-operation and marketing agreement’ in respect of the operation of a service station.⁶⁸ Under its terms Yötuuli Ky undertook to exclusively sell Neste’s oil and other products. It was concluded for a period of ten years, after which it would continue for periods of five years, unless terminated by either party.⁶⁹ Termination was effected through the provision of notice to the other party six months before the end of the term of the contract.⁷⁰ However, once the agreement had run for a term of ten years or more the purchaser, Yötuuli Ky, could at any time terminate the agreement on the provision of one year’s notice.⁷¹ On providing such notice, Neste brought a claim for compensatory damages. Yötuuli Ky claimed the exclusive purchasing obligation was contrary to Article 101(1) TFEU as the agreement was precluded from exemption under Regulation 1984/83 as it continued automatically and so was for an ‘indefinite duration’. They claimed it was therefore void under Article 101(2) TFEU.⁷² The national court subsequently sought a preliminary ruling. This was sought on the interpretation of Article 101(1) TFEU, in light of the CJEU’s ruling in *Delimitis*,⁷³ presupposing that Neste’s exclusive purchasing agreements, along with parallel networks of similar agreements, had significant market foreclosing effects.⁷⁴ However, agreements terminable on one year’s notice, such as that concluded with Yötuuli Ky, constituted only a small proportion of Neste’s agreements with only 1.5% of service stations in Finland being tied to Neste in this way.⁷⁵

In its written observations submitted to the CJEU, the Commission appeared to adopt a firmer stance than that evident in its practices concerning beer supply agreements. It stated “*the fact that the effects on competition of an individual contract or group of contracts are relatively insignificant does not mean that such a contract or group of contracts is not caught by Article [101(1) TFEU].*”⁷⁶ It subsequently stated that Neste’s network of agreements should not be sub-divided on the basis that these agreements made an

⁶⁷ The central issue in the preliminary reference was whether the effects of certain agreements which could be freely terminated following a short notice period could be assessed separately from the supplier’s other fixed duration agreements. Ibid at para A1, p996-997

⁶⁸ Ibid at para A2, p997

⁶⁹ Ibid at para A2, p997

⁷⁰ Ibid at para A2, p997

⁷¹ Ibid at para A2, p997

⁷² Ibid at para A4, p997-998

⁷³ Chapter 3, p77

⁷⁴ Above, n.66 at para A16, p1002

⁷⁵ Ibid at para 29, p1016. See also A Crowe, ‘Case Comment: Petrol service station network – Exclusive purchasing Agreements’ (2001) 22(4) E.C.L.Rev N58 at N59

⁷⁶ Above, n.66 at para A12, p1000. This is a firmer stance than that exemplified by the Commission’s approach towards the beer supply agreements of small brewers in the EEC Beer Review. There it suggested that such agreements be subject only to national law. The Commission stated that this was so even where parallel agreements of other brewers existed. Chapter 3, p74-76

insignificant contribution to the cumulative effect of all Neste's arrangements. To do so would be arbitrary and contrary to the CJEU's approach in *Delimitis*.⁷⁷ Such an approach was expressly rejected by the General Court in *Langnese-Iglo*⁷⁸ and *Scholler*,⁷⁹ the only case where the benefit of block-exemption has been withdrawn.⁸⁰ The Commission therefore asserted that a bundle of similar agreements had to be considered as a whole. Nevertheless, the CJEU departed from this approach.

Following *Delimitis*, the CJEU focused on whether Neste's agreements combined with other agreements have a cumulative effect on competition and make access to the relevant market difficult;⁸¹ and examined whether the agreements in question contributed to the "cumulative effect produced by the totality of the agreements".⁸² However, the CJEU agreed with Neste's position that exclusive purchasing obligations for fuels differed in one significant respect from those for other products, including beer and ice-cream.⁸³ Service stations sell only one brand of fuel.⁸⁴ In light of this, the duration of the supply obligation of the reseller is more important to the supplier than the exclusivity clause and is the decisive factor in the market sealing-off effect.⁸⁵ The CJEU stated that it had to be acknowledged that fixed-term contracts concluded for a set number of years were more likely to limit access to the market than those terminable on one year's notice.⁸⁶ The CJEU noted the onerous obligations in terms of investment, amongst other things, involved in adapting a service station to its brand.⁸⁷ As such, the CJEU opined that a one-year notice period protected the economic and legal interests of the parties and provided suppliers, and their investment, with reasonable protection.⁸⁸ This was also considered to have only a limited restrictive effect on competition on the market in motor fuel distribution.⁸⁹

⁷⁷ Ibid at para A12, p1000.

⁷⁸ (T-7/93) *Langnese-Iglo v. E.C. Commission* [1995] ECR II-1533; [1995] 5 CMLR 602

⁷⁹ (T-9/93) *Schöller Lebensmittel v. E.C. Commission* [1995] ECR II-1611 and above, n. 66 at para A12, p1000

⁸⁰ *Langnese/Schöller* concerned exclusive purchasing agreements for ice-cream concluded with retailers and resulted in the withdrawal of exemption for such agreements under Regulation 1984/83. The General Court stated that "[t]he Court considers...that a bundle of similar agreements must be considered as a whole and, therefore, that the Commission was right not to examine the agreements separately". (*Langnese-Iglo* [1995] 5 C.M.L.R.602 at para 131, p643). This was upheld on appeal to the CJEU. (Case C279/95P) *Langnese-Iglo v. Commission* [1998] ECR I-5609).

⁸¹ Above, n.66 at para 25-26, p1015-1016

⁸² Ibid at para 27, p1016

⁸³ Ibid at para 31, p1017

⁸⁴ Ibid at para 31, p1017

⁸⁵ Ibid at para 32, p1017

⁸⁶ Ibid at para 33, p1017

⁸⁷ Ibid at para 34, p1017

⁸⁸ Ibid at para 35, p1017

⁸⁹ Ibid at para 35, p1017

In light of the foregoing circumstances of the case the CJEU considered that the contracts in question constituted a minor proportion of all of Neste's exclusive purchasing agreements. As such, they had to be regarded as making no significant contribution to the cumulative effect for the purpose of *Delimitis*, and so, were outside the scope of Article 101(1) TFEU.⁹⁰ The CJEU proceeded to justify this position as being compatible with *Delimitis*. It stated that although that judgment established the criteria for “*assessing the extent to which a supplier's “contracts”, without being more specific, contribute to the cumulative sealing-off effect, it did not exclude a selective assessment according to the various categories of contract that a particular supplier might have entered into*”.⁹¹ Whilst this may be the case, Cumming correctly suggests that the CJEU's judgment in *Neste* appears to undermine the certainty of the *Delimitis* network concept when considering the anticompetitive effect of individual agreements.⁹² Having determined that the agreement in question forms part of a network as required, the CJEU introduces the need for a selective assessment of the various categories of contract the supplier has entered into. Cumming considers that the decision means it “*is simply no longer possible to predict the status of an individual agreement in relation to Article [101(1) TFEU] by applying the concept of the network*.”⁹³ It is however suggested here that this was not the case even under *Delimitis*. As noted in Chapter 3, the CJEU established two cumulative conditions when assessing the legality of an agreement. These required that the agreement in dispute not only forms part of a network of agreements but also makes a significant contribution to the cumulative effect of those agreements. Simply being part of a network of agreements was not sufficient to determine the status of an agreement under the *Delimitis* conditions and the CJEU in *Neste* did not deviate from this position. It simply muddled the waters. Nevertheless, the overall effect of the CJEU's judgment in *Neste* would appear to be a reduction of the scope of Article 101(1) TFEU to exclusive purchasing obligations, with Cumming and Ratliff supporting this view.⁹⁴ The CJEU, however, appears to have specifically limited its judgment to a restricted context, namely where the agreement is entered into by a motor fuels supplier; termination is possible on one year's notice thereby ensuring adequate protection to both parties; and the agreements at issue, by reason of their

⁹⁰ Ibid at para 36, p1017

⁹¹ Ibid at para 38 p1018

⁹² G Cumming, ‘Case Comment Neste Markkinointi Oy and Yötuuli Ky’ (2001) 22(9) E.C.L.Rev 394 at p397

⁹³ Ibid at p397

⁹⁴ Ibid at 399. See also J Ratliff, ‘Major events and policy issues in EC competition law, 2001: Part 1’ (2002) 13(1) I.C.C.L.R 6 at p12. Ratliff states that *Neste* highlights that the requirement for a “*significant contribution to sealing off the market*” is to limit the number of agreements being declared void on the basis of competition considerations.

duration, represent a very small part of the totality of one supplier's exclusive purchasing agreements, the majority being fixed term contracts entered into for more than one year.⁹⁵

2.1.4 Regulation 2790/99 – a more economics-based approach to service station agreements

Nevertheless, as discussed in Chapter 3,⁹⁶ calls for a generally more economics-based approach to the handling of vertical agreements, including those in the beer and petrol industries, resulted in the replacement of the sector specific rules of Regulation 1984/83 with Regulation 2790/99.⁹⁷ As noted in Chapter 3, this was applicable to all vertical restraints concerned with intermediate and final goods, as well as services, with the exclusion of only a few hardcore restraints.⁹⁸ However, the new Regulation introduced a market share cap for the first time. Where the market share of the supplier did not exceed 30%, and the vertical agreement did not contain any of the 'black' listed provisions they were generally considered to lead to an improvement in distribution or production and allowed consumers a fair share of the resulting benefit.⁹⁹ Consequently, following the implementation of Regulation 2790/99, as in the beer market, in the petrol market occasions arose when the market share cap was breached, causing the Commission to be notified of agreements that would have benefitted from exemption under Regulation 1984/83.

Similarly to Interbrew, which as discussed in Chapter 3 had to notify its tying agreements to the Commission following the adoption of Regulation 2790/99, Repsol, a major distributor of fuel and related products in Spain, notified it of its Spanish service station agreements that included non-compete obligations.¹⁰⁰ The Commission invited observations from interested parties with several being received.¹⁰¹ Repsol had a market share of 35-50% of the relevant market.¹⁰² In its Notice published in 2004, the Commission highlighted its competition concerns and remedies. Amongst its concerns, the Commission

⁹⁵ Above, n.66 at p1019

⁹⁶ Chapter 3, p88-90

⁹⁷ Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices ((1999) OJ L336/21)

⁹⁸ The terms of Regulation 2790/99 are discussed in Chapter 3 and are equally applicable to petrol station agreements. Chapter 3, p90

⁹⁹ A new *de-minimis* notice was also published and potentially provided a safe harbour to petrol station agreements. Chapter 3, p96

¹⁰⁰ European Commission, *Notification of agreements (Case COMP/38.348/E3 (Repsol CPP SA – Distribution of motor fuels))* ((2002) OJ C70/29)

¹⁰¹ 69 observations were received. Final Report of the Hearing Officer in Case COMP/B1-38.348 *Repsol* ([2006] OJ C152/6)

¹⁰² European Commission, Notice pursuant to Article 27(4) of Council Regulation No 1/2003 concerning Case COMP/B-1/38348 Repsol CPP SA ((2004) OJ C258/7) at para 11, 8

noted the non-compete clauses in Repsol's agreements, the duration of which in some agreements was five years, while in its tenancy type agreements it ranged from 25-40 years.¹⁰³ The Commission also had concerns over the foreclosure effect of the non-compete obligations and their weakening of inter-brand competition in the relevant market.¹⁰⁴ It noted, amongst others, the difficulty experienced by competitors attempting to access the market or increase their market share due to the significant vertical integration of operators, and the cumulative effect of the parallel network of such agreements.¹⁰⁵ The Commission considered that the notified agreements potentially contributed significantly to the foreclosure effect due to the extent of the non-compete obligations imposed; the substantial duration of these non-compete obligations; and the 'weak and fragmented' position of services station operators and final consumers by comparison to suppliers such as Repsol.¹⁰⁶ Numerous commitments were offered by Repsol, including observing a five-year duration limit on new agreements and an undertaking not to purchase service stations that were not tied to its network.¹⁰⁷ Whilst the Commission considered these commitments provided a 'practical response' to the concerns raised, responses to the notice called their effectiveness into question.¹⁰⁸ Repsol submitted amended commitment proposals which were revised several times, with the Commission ultimately accepting them as no longer presenting grounds for action under the EU competition law provisions.¹⁰⁹ Consequently, as was the case when dealing with Interbrew's notified agreements,¹¹⁰ the Commission was prepared to accept the single branding obligation despite Repsol's very significant market share.

Further, despite the new economics-based approach of Regulation 2790/99, the deference towards beer and service station agreements at the EU level was also maintained. As discussed in Chapter 3, Article 5(a) of Regulation 2790/99 denied exemption to non-compete obligations of indefinite duration or in excess of 5 years reflecting on-going concerns over the duration of such obligations and their foreclosure effects.¹¹¹ However this was not applicable to beer and service station agreements under which the goods were sold from premises and land owned or leased by the supplier, with such agreements

¹⁰³ Ibid at para 21, 9

¹⁰⁴ Ibid at para 22-23, 9

¹⁰⁵ Ibid at para 23, 9

¹⁰⁶ Ibid at para 24, 9

¹⁰⁷ Ibid at para 26, 10

¹⁰⁸ Ibid at para 28, 10 and above, n.101

¹⁰⁹ *Repsol* [2006] OJ C152/6

¹¹⁰ Chapter 3, p95

¹¹¹ Chapter 3, p98

continuing to qualify for exemption.¹¹² The non-compete obligation simply could not exceed the period of occupation of the premises.

The CJEU in *Pedro IV Servicios*¹¹³ gave a preliminary ruling on the eligibility of an exclusive purchasing agreement between a service station operator and a petrol supplier under Regulation 2790/99. The CJEU disagreed with the submissions from the Commission that Regulations 1984/83 and 2790/99 must be interpreted in the same way, even although they are drafted differently. The Court found that Regulation 2790/99 clearly required that the supplier owned both the land and the premises from which the contractual goods were sold by the reseller.¹¹⁴ The CJEU stated that Article 5(a) had been drafted in clear and unequivocal terms.¹¹⁵ In contrast to the position under Regulation 1984/83, for the purposes of applying Regulation 2790/99, a service station agreement lasting longer than five years could only benefit from exemption if the supplier is both the owner of the service station which he lets to the reseller and also owns the land on which it is built. If the supplier is not the owner, he must lease the land and the service station from third parties unconnected to the reseller.¹¹⁶ Regulation 2790/99 therefore tightened up on the position under Regulation 1984/83 however beer and service station agreements of longer durations than were permitted in other sectors of the economy continued to benefit from exemption.

2.1.5 Regulation 330/2010

As noted in Chapter 3, as the expiry of Regulation 2790/99 loomed, it was considered to have worked well with no drastic measures being proposed to the system it implemented.¹¹⁷ Under its successor Regulation 330/2010,¹¹⁸ the greatest change required that both the supplier and the buyer's market share of the relevant market did not exceed 30% in order to qualify for exemption.¹¹⁹ Similarly to the responses received from the brewing industry,¹²⁰ this was not well received by the petrol industry. BP highlighted their concerns over the practical difficulties this would cause without resulting in efficiency gains. They were concerned it would narrow the application of the Regulation and lead to

¹¹² Article 5(a) Regulation 2790/99

¹¹³ (C-260/07) *Pedro IV Servicios SL v. Total España SA* [2009] ECR I-2437; [2009] 5 CMLR 1291

¹¹⁴ (C-260/07) *Pedro IV Servicios SL v. Total España SA* [2009] 5 CMLR 1291 at para 44, p1331

¹¹⁵ *Ibid* at para 51, p1331

¹¹⁶ *Ibid* at para 69, p1333

¹¹⁷ Chapter 3, p100-101

¹¹⁸ Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices ((2010) OJ L102/1)

¹¹⁹ Article 3, Regulation 330/2010. Chapter 3 at p101

¹²⁰ Chapter 3, p102

legal uncertainty.¹²¹ BP was also concerned that whilst larger suppliers are aware of their market shares, they often have no knowledge of the buyer's downstream market and must rely on their share being below 30% to enforce the non-compete obligation.¹²² They subsequently stated that buyers have little incentive to assist in their diligence as an over-statement of their market shares would render the obligation unenforceable.¹²³

Article 5(2) of Regulation 330/2010 however maintained the status quo for beer and service station agreements by exempting them from the 5-year time limit on non-compete obligations where the goods or services are sold by the buyer from premises and land owned by the supplier or leased by the supplier. Again, it requires simply that the duration of the non-compete obligation does not exceed the period of occupancy of the premises. Consequently, the deference of the past towards beer and service station agreements is still evident in the terms of the current BER.

2.2 EU's influence on UK competition authorities' approach to both sectors

This deference at the EU level has subsequently filtered through to the UK competition authorities' approach to the beer and petrol industries. As discussed in Chapter 4, the UK competition law regime was largely harmonised with the EU competition provisions through the enactment of the Competition Act 1998 and the Enterprise Act 2000. As discussed in Chapter 4, the Chapter I prohibition of the Competition Act 1998 reflects Article 101(1) TFEU and forbids agreements, decisions by associations of undertakings and concerted practices which affect trade in the UK and have as their object or effect the restriction of competition in the UK. Consequently, this is applicable to beer tie and solus agreements. However, s.60 of the 1998 Act requires consistency in the application of national and EU competition law with conformity also being ensured by s.10 of the 1998 Act which provides for parallel exemptions, thereby importing all EU block exemptions into national law.¹²⁴ Consequently, as will be shown, the UK competition authorities have often deferred to the EU's acceptance of beer tie and solus agreements as legitimate business models when considering complaints regarding the practices within the retail distribution of beer and petrol in the UK. The complaints have been numerous and on-

¹²¹ 'British Petroleum, 'The Commission's proposed amendments to the Vertical Restraints Block Exemption Regulation (VRBER) and Guidelines Submission from BP plc' at para 3, Introduction (*Europa*, September 2009) <http://ec.europa.eu/competition/consultations/2009_vertical_agreements/bppic_en.pdf> accessed 19th February 2015

¹²² Ibid at para 4.b, Introduction

¹²³ Ibid at para 4.b, Introduction

¹²⁴ Chapter 4, p113-114

going in both industries, with continuing mistrust over their operation prompting many investigations into both sectors for several decades by the UK competition authorities. However, as will become evident from the following review of their findings, with the exception of the Beer Orders, the authorities seem to have been similarly unable to identify anticompetitive behaviour in either sector.

3. Numerous and on-going competition concerns in both sectors

As discussed in Chapters 2 and 4, there have been numerous investigations into the practices employed in the retail distribution of beer, both before and after the radical structural shake-up brought about by the Beer Orders in 1989. Similarly, the retail distribution of petrol has also been subject to considerable attention by the UK competition authorities, with on-going mistrust over the operation of both of these markets prompting repeated recommendations that they be kept under review. Although, as will be shown the petrol industry has escaped any sweeping recommendations along the lines of the Beer Orders, several investigations have been conducted since the Monopolies and Mergers Commission's (MMC)¹²⁵ first report in 1965 on the supply of petrol in the UK.¹²⁶ Whilst the focus of these investigations in the beer industry remains the operation of the tie and its implications, albeit as now operated by pubcos not brewers; over the decades the focus within the petrol industry has shifted from concerns over high levels of vertical integration, to the increasing dominance of supermarkets in the retail sale of petrol. Despite the interest shown in the operation of both sectors however they have been repeatedly cleared of anticompetitive practices. Nevertheless, as already discussed in Chapter 2, in the earliest reports prior to the UK's accession to the EU in 1973, given the EU and UK's differing objectives at that time, these were more scathing than the most recent investigations focused on the practices of pubcos and supermarkets respectively.

3.1 Early common concerns over vertical integration and monopoly situations

3.1.1 Concerns over vertical integration in both sectors

The MMC was one of the first bodies to consider the practices within the brewing and petrol industries, reviewing the former in 1969,¹²⁷ and the latter in 1965.¹²⁸ As discussed in

¹²⁵ Then known as the Monopolies Commission.

¹²⁶ J.F. Pickering, 'Competition policy and vertical relationships: the approach of the UK Monopolies and Mergers Commission' (1999) 20(4) E.C.L.Rev 225 at 229

¹²⁷ Chapter 2, p27

¹²⁸ Above, n.2

Chapter 2, its report on the brewing industry focused on the level of vertical integration, with this also being the focus when considering the supply of petrol to retailers in the UK.¹²⁹ The high levels of vertical integration prompted similar concerns in relation to both, including the fear that these arrangements dampened price competition amongst public houses and petrol stations in their respective markets.¹³⁰ As discussed in Chapter 2, the MMC was far more critical of the tied house system, finding that it was detrimental to efficiency and to the interests of suppliers and consumers. It subsequently concluded that “...a state of affairs in which brewers did not own or control licensed outlets would be preferable to the tied house system”.¹³¹ However, it conceded that restrictive licensing of public houses reduced competition by limiting the establishment of new competitors, prompting recommendations that the licensing laws be amended to address the ‘defects’ of the tied house system.¹³² Further, when considering the issue of the solus system, although the MMC was less scathing than it was in respect of the beer tie, ultimately stating that it approved of it in principle, it considered that as the system operated in the UK at that time, it had “some disadvantageous features”.¹³³ Whilst in its preliminary conclusions it accepted that the solus system had, amongst others, led to some reductions in suppliers’ costs and reduced retail prices, it concluded that the restrictive agreements between petrol suppliers and retailers was contrary to the public interest.¹³⁴ The solus agreements used were considered too long; too wide; contained provisions relating to lubricants and non-petroleum based products; enabled suppliers to exert too much influence over the retailers’ trade in those products to their own advantage; and granted the supplier rights of pre-emption in the sale of the premises.¹³⁵ It was therefore recommended that they be limited in duration to five years;¹³⁶ and recommendations were made to address the other concerns noted. These included preventing suppliers’ committing retailers to sell specified quantities of lubricants, and precluded suppliers’ from accepting commission in relation to the sale of non-petroleum based products.¹³⁷ It was also concluded that company ownership could operate against the public interest if limits were not imposed on this, and so it was recommended that the largest suppliers should not be allowed to acquire any further petrol

¹²⁹ In the petroleum market, by the end of 1964 it was estimated that 95% of all petrol stations in the UK sold the brands of a single supplier. Above, n.2 at para 101, p35

¹³⁰ Ibid at para 346-349, p129-130

¹³¹ Chapter 2, p28

¹³² Chapter 2, p28-29

¹³³ Above, n.2 at para 424, p157

¹³⁴ Ibid at para 379, p141 and para 427, p158-159

¹³⁵ Ibid at para 427(3)(a), p159

¹³⁶ The 5-year term was subject to the option of continuity on an annual basis (ibid at para 428(1), p159). The exceptions to the duration limit were situations where there was a lease or loan agreement in place (ibid at para 428(8), p160-161)

¹³⁷ Ibid at para 428(4) and (5), p160

stations, or interests in them.¹³⁸ Nevertheless, despite these recommendations, given the control exerted in both industries by the major brewers and oil companies concerns within both turned to the possible existence of a monopoly situation.

3.1.2 Early concerns over monopoly in both sectors

As discussed in Chapter 2, the brewing industry was reviewed by the Price Commission in 1977 over concerns of vertical, as well as horizontal, integration as the price of beer continued to increase.¹³⁹ Not long afterwards, in 1979 the MMC investigated the possible existence of a monopoly situation in the petrol industry.¹⁴⁰ With regard to the brewing industry, its highly concentrated nature combined with high barriers to entry, were considered by the Price Commission to be the ‘classic conditions’ for a monopoly.¹⁴¹ The lack of price competition was highlighted, with the combined effects of high concentration and vertical integration enabling managed houses to lead prices upwards.¹⁴² The primary concern was therefore the closed nature of trade and the diminishing level of price competition due to the extensive use of the beer tie. Similarly, the MMC’s 1979 review of the possible existence of a monopoly in the supply of petrol considered price competition between retail outlets and company ownership of these.¹⁴³ By contrast to the increasingly concentrated brewing industry, the MMC noted that since its report in 1965, the number of companies producing petrol had increased and the growth of smaller suppliers had also improved.¹⁴⁴ However, whilst this had stimulated greater price competition as the new entrants adopted different pricing policies from the established majors,¹⁴⁵ they also introduced temporary discounts and financial support, known as Selective Price Support (SPS), in order to address increasing petrol prices, with other refining wholesalers soon following suit.¹⁴⁶ This support varied depending on the market conditions, targeting the areas of greatest competition and reflecting the uneven nature of price competition.¹⁴⁷ Whilst the aim had been to regain volumes this ultimately caused regional price variations.

¹³⁸ This was imposed on suppliers whose deliveries to company-owned stations exceeded 15% of total deliveries to petrol stations in that year (ibid at para 428(7), p160)

¹³⁹ Chapter 2, p29-30

¹⁴⁰ The Monopolies and Mergers Commission, *Petrol a report on the supply of petrol in the UK by wholesale* (Cmnd 7433, 1979)

¹⁴¹ Chapter 2, p29-30

¹⁴² Chapter 2, p30

¹⁴³ Above, n.140 at para 1, p1. It also considered promotional schemes of wholesalers, however the focus here is the factors contributing to the monopoly situation.

¹⁴⁴ Ibid at para 45, p20-21. New entrants included refining wholesalers Burmah, ICI and Chevron and independent wholesalers lacking refining capacity.

¹⁴⁵ Ibid at para 46, p21. New entrants offered retailers similar scheduled prices to the established majors but offered more substantial solus rebates.

¹⁴⁶ Ibid at para 54 and para 57, p23

¹⁴⁷ Ibid at para 55, p23

The MMC subsequently found that this affected competition between retailers,¹⁴⁸ and amounted to “*discrimination in net wholesale prices in response to the severity of local retail price competition*”.¹⁴⁹ Further, similarly to the concerns over vertical integration in the brewing industry, the MMC noted that solus agreements were still widespread, and concluded that a monopoly situation existed in relation to the supply of petrol by wholesale in the UK.¹⁵⁰ However, due to the reduction in seller concentration and the increase in the number of refining and non-refining competitors,¹⁵¹ the level of company ownership of retail outlets did not operate against the public interest.¹⁵² Nevertheless it was again recommended that the level of company ownership and seller concentration be kept under review.¹⁵³ Concerns over the possible existence of a monopoly situation did not dissipate and shortly after its consideration of the brewing industry in 1989 the MMC duly revisited the petrol industry, although this failed to prompt any recommendations along the lines of the Beer Orders.

3.2 MMC review of beer and petrol industries

In the late 1980s, not long after the implementation of Regulation 1984/83, the MMC investigated the brewing and petrol industries. Whilst critical of the supply of petrol, its report was not as far reaching in its recommendations as it was in respect of the brewing industry.¹⁵⁴ As discussed in Chapter 2, its concerns over the level of brewery ownership of retail outlets contributed to its finding that a complex monopoly existed in favour of brewers with tied estates, and restricted competition at all levels. This prompted it to recommend a cap of 2,000 on the number of licensed premises that any brewer could own.¹⁵⁵ Similarly, its investigation in the petrol industry was necessitated by concerns over

¹⁴⁸ Ibid at para 133, p52

¹⁴⁹ Ibid at para 130, p51. A monopoly situation existed in the supply of petrol in the UK by wholesale under s.6(1)(c) Fair Trading Act 1973 as at least one quarter of the petrol supplied by wholesale was supplied by persons operating SPS, which discriminated between retailers in respect of the prices or the terms on which they were offered or supplied petrol (above, n.140 at para 151, p56). However, as outlawing this would have required agreements between wholesalers and retailers to be supervised by a regulatory body, SPS was not considered contrary to the public interest (above, n.140 at para 135, p52).

¹⁵⁰ At least one quarter of petrol supplied by wholesale was supplied by persons who had secured exclusive retail outlets by acquiring proprietary interests in them and required that only petrol they supplied be sold at them (above, n.140 at para 151, p56).

¹⁵¹ Ibid at para 144-145, p54. As noted above, the 1965 Report recommended that controls be placed on company ownership of retail outlets as otherwise this would operate against the public interest. The MMC stated that this recommendation was based on concerns that such ownership could lead to “*rigidity*” in the retail trade and between suppliers. Since that report, the structure of the wholesale supply had changed due to new market entrants.

¹⁵² Ibid at para 148, p55 and para 152, p56-57

¹⁵³ Ibid at para 149, p55-56

¹⁵⁴ Chapter 2, p30

¹⁵⁵ Chapter 2, p36

the degree of vertical control being exerted within it.¹⁵⁶ The MMC noted that the retail petrol market was supplied by 69 wholesalers, with many of the fourteen major players on the market at that time also being involved in oil exploration and refining.¹⁵⁷ Similarly to the six national brewers at that time, these wholesalers also owned a significant number of retail sites and also supplied independent retailers.¹⁵⁸ However, as in 1965, the MMC did not find the principle of the solus tie to be objectionable and noted that, in contrast to the beer tie, there had been no suggestion that its use be abandoned.¹⁵⁹ Nevertheless, in considering the competitive situation in the petrol distribution sector the MMC addressed issues that were also common to the brewing industry, such as the increasing company ownership of retail outlets, control of retail prices, and the possible existence of a monopoly situation.

3.2.1 Ownership of outlets – a common problem

As discussed in Chapter 2, brewery ownership of public houses was one of the principle drivers in the MMC's finding that a complex monopoly situation existed in the UK market. However, in considering wholesaler ownership of petrol stations, it was noted that since 1977 the proportion of sites owned by them had only increased slightly, as had the sales by volume through them.¹⁶⁰ Whilst as discussed in Chapter 2 the MMC had estimated that 75% of all public houses in Great Britain were owned by brewers, it was estimated that only 33.2% of petrol stations were owned by wholesalers.¹⁶¹ Nevertheless, the MMC received complaints that wholesalers' control over both prices and the means of operation of sites dampened competition at the retail level and inhibited licensees from lowering prices or responding to local consumer needs.¹⁶² The MMC however attributed licensees' difficulty in cutting prices to the higher wholesale price they paid for petrol by comparison to independent retailers, with this being justified by the significant investment wholesalers had to make in retail sites.¹⁶³ Further, the control exerted was part of the wholesaler's broader strategy to establish and promote their brand, thereby promoting not inhibiting competition.¹⁶⁴ In contrast to the brewing industry, the MMC therefore concluded that

¹⁵⁶ Above, n.14 at para 1.1, p1. The House of Common's Select Committee on Trade and Industry initiated an inquiry into the UK petrol retailing industry. Due to the significant contradiction in the evidence received from oil companies and retailers, it deferred to the MMC noting the possibility that the prevailing complex monopoly was limiting competition and was contrary to the public interest (ibid at para 2.7, p9).

¹⁵⁷ Ibid at para 1.30, p5 and para 1.3, p1

¹⁵⁸ Ibid at para 1.4, p1

¹⁵⁹ Ibid at para 1.17, p3

¹⁶⁰ Wholesaler ownership had only increased from 30% to 33% (above, n.14 at para 8.104, p293).

¹⁶¹ As at 1988 (above, n.14 at Table 3.13, p38)

¹⁶² Above, n.14 at para 1.22, p4

¹⁶³ Ibid at para 1.23, p4

¹⁶⁴ Ibid at para 1.23, p4

wholesaler ownership and the way in which they operated petrol stations did not have an adverse effect on competition.¹⁶⁵

3.2.2 Control of retail prices – a problem shared

Similarly to brewers who exerted significant influence over retail prices through both their wholesale price and the prices charged at their managed houses, petrol wholesalers also exerted significant influence over the pump prices charged at their petrol stations.¹⁶⁶ However, whilst as discussed in Chapter 2 the MMC's 1989 report concluded that amongst others the complex monopoly situation that existed in favour of brewers had caused the price of a pint of beer to rise too quickly in recent years, had allowed regional price variations, and the increased cost of lager was not justified by the cost of production, similar conclusions were not reached with regard to the distribution of petrol.¹⁶⁷ At the outset of its report on the petrol industry, the MMC noted that numerous factors influenced the retail price of petrol.¹⁶⁸ Whilst it was established that pump prices could vary from one site to another within local areas and across the country,¹⁶⁹ the MMC considered that this was attributable to the differing range of services offered at different sites, although wholesalers were also highly influential through the wholesale prices they set and their use of SPS.¹⁷⁰ Nevertheless, the MMC was satisfied that the extent to which these could be used to maintain higher prices was limited by competition from other wholesalers, independent sites and supermarkets.¹⁷¹ It therefore concluded that regional price differences were due to variations in the level of local competition.¹⁷² Further, in considering price differences in rural areas compared with central locations, these were not attributed to excessive profit margins but were due to the higher costs of supply and reduced competition at the wholesale and retail level.¹⁷³ Consequently, the price increases in the supply of petrol were not as contentious as those in the supply of beer.

¹⁶⁵ Ibid at para 1.24, p4

¹⁶⁶ Ibid at para 1.25, p4

¹⁶⁷ Chapter 2 at p32-35

¹⁶⁸ Unlike beer, petrol is an internationally-traded commodity with petrol prices being influenced by movements in international crude oil markets (above, n.14 at para 4.1, p61).

¹⁶⁹ Ibid at para 8.131, p298

¹⁷⁰ Ibid at para 1.25, p4

¹⁷¹ Ibid at para 1.25, p4

¹⁷² Ibid at para 1.26, p4

¹⁷³ Ibid at para 1.27, p5. The MMC also considered the potential for new entrants at the wholesale level. Although constraints existed such as planning and safety regulation, these had not prevented entry or expansion into the market at various levels over the recent past. Consequently no recommendations were made in this regard. (Ibid at para 1.28, p5)

3.2.3 No equivalent of the Beer Orders for the petrol industry

Following its consideration of similar issues in both industries, the MMC reached different conclusions in respect of them. As discussed in Chapter 2, the MMC concluded that a complex monopoly existed in favour of brewers with tied estates or loan ties with free houses and restricted competition at all levels.¹⁷⁴ This prompted far reaching structural remedies in the form of the Beer Orders. However, with regard to the supply of petrol the MMC found that unlike the national brewers, the principal wholesalers competed effectively on price, facilities and services.¹⁷⁵ In most areas consumers were thought to have a wide range of petrol prices and services to choose from and UK pump prices after tax were generally not unreasonable compared against European pump prices.¹⁷⁶ The profits enjoyed by companies in their wholesale operations had been moderate¹⁷⁷ and since its last report there had been a reduction in concentration with the combined market share of the five oil majors declining, with the entry of new wholesalers to the UK market being noted.¹⁷⁸ The MMC highlighted the rise of supermarkets as a strong competitor and stated that annually significant numbers of independent solus contracts were replaced causing wholesalers to compete for these, thereby strengthening the position of independent retailers.¹⁷⁹ In contrast to the brewing industry, all of these factors assisted in maintaining prices and services at a competitive level.¹⁸⁰ Consequently, intervention along the lines of the Beer Orders was not necessary, however, as before the MMC highlighted that it would be nervous about a significant increase in wholesaler ownership of petrol stations or the volume of fuel sold through them.¹⁸¹ As a result, the market was once again monitored.¹⁸²

4. Structural changes and continued declarations of competitiveness in the UK beer and petroleum markets

Both the UK beer and petrol markets therefore continued to be monitored and reviewed. However, following the structural changes in the beer market resulting from the MMC's

¹⁷⁴ Chapter 2, p32

¹⁷⁵ Above, n.14 at para 1.34, p6

¹⁷⁶ Ibid at para 1.32, p5

¹⁷⁷ Ibid at para 1.33, p6

¹⁷⁸ Ibid at para 1.34, p6

¹⁷⁹ Ibid at para 1.34, p6

¹⁸⁰ Ibid at para 1.34, p6

¹⁸¹ Ibid at para 1.36, p6

¹⁸² Ibid at para 1.38, p6. Whilst the brewing industry was undergoing significant structural reforms following the Beer Orders, in 1993 the petrol industry was reviewed by the OFT. Its report was not made public, however its primary revelation was that the oil majors were losing market share to supermarket chains. The Director General of Fair Trading found that the market was operating as the MMC had found it and scheduled a review for 1997. Office of Fair Trading, *Competition in the supply of petrol in the UK* (OFT 230, 1998) at para 4.3, p13

recommendations, the focus turned to the practices of pubcos, in the place of national brewers; and due to their increasing market presence, supermarket forecourts instead of oil companies in the supply of petrol. Nevertheless, as will be shown, both would benefit from on-going declarations of competitiveness. This was the case when in 1998 the OFT reported on the retail distribution of petrol and shortly afterwards, in 2000, declared the retail distribution of beer sufficiently competitive for the Beer Orders to be revoked. Subsequently, the structural changes that had occurred in both markets were seen to have enhanced not inhibited competition.

4.1 Pubcos and increasing retail prices but improved market entry at the retail level of the UK beer market

As discussed in Chapter 2, when considering whether or not the Beer Orders were still required, the OFT highlighted the significant structural changes that had been brought about in the retail distribution of beer due to the substantial growth in pubco ownership of public houses. Pubcos now owned over one third of the UK's public houses and were found to enjoy a degree of countervailing buyer power in relation to the national brewers.¹⁸³ Whilst this power was found to have enabled pubcos to negotiate reductions in the average net wholesale price of beer, this had not filtered through to the retail price of beer in the on-trade, which was continuing to increase.¹⁸⁴ The OFT did not however attribute this to a failure in retail competition. Rather, it considered that retail competition in the supply of beer was manifest in increased levels of capital expenditure on amenity and service provision.¹⁸⁵ It also considered that consumers now had a greater choice of different price and amenity combinations due to the emergence of low-priced retail pub chains.¹⁸⁶ However, as already discussed in Chapter 2, by contrast to the wholesale supply of petrol an independent wholesale and distribution sector had not materialised in the UK beer market. The majority of beer sold to the on-trade continued to be distributed by the national brewers, who could exert significant control through their distribution channels.¹⁸⁷ Nevertheless, the OFT considered that the distinction between pubs and other on-trade outlets had been clouded, with pubs increasingly competing with clubs, bars and to some extent restaurants.¹⁸⁸ It was subsequently satisfied that overall the UK market was sufficiently different at all levels of the supply chain compared to before the Beer Orders

¹⁸³ Chapter 2, p42-43

¹⁸⁴ Chapter 2, p44

¹⁸⁵ Chapter 2, p44

¹⁸⁶ Chapter 2, p44

¹⁸⁷ Chapter 2, p43

¹⁸⁸ Chapter 2, p44

and recommended that they be revoked subject to the retention of certain provisions.¹⁸⁹ Nevertheless, there was some acknowledgement by the OFT that competition in the market could be improved and so it continued to be subject to review. As discussed in Chapter 4 however the OFT attempted to resist further investigations into the concentration of public house ownership in the hands of pubcos on the basis that the beer tie did not infringe the EU competition provisions.¹⁹⁰

4.2 Increasing supermarket forecourts but decreasing pump prices and diversity of suppliers in the UK petroleum market

However, shortly before it recommended the revocation of the Beer Orders, the OFT considered competition in the supply of petrol in the UK. Similarly to the rise of the pubco in the distribution of beer, it noted that since 1990 the market share held by supermarket forecourts had significantly increased from 5% to approximately 23%.¹⁹¹ Their growth had encouraged oil companies to diversify into alternative product lines, such as shopping facilities, and forced them to focus on their high volume sites,¹⁹² as supermarkets tended to operate very large forecourts, with substantial throughputs.¹⁹³ This strategy enabled supermarkets to spread the high fixed costs of operating a forecourt and so allowed them to charge very competitive retail prices for fuel.¹⁹⁴ Consequently, in contrast to pubcos which as discussed in Chapter 4 were driving up retail beer prices, supermarkets placed downward pressure on petrol prices. Since 1990, these had been cut by approximately one third, with a significant improvement also being made in the services offered at forecourts.¹⁹⁵ However the corollary of this was a marked reduction in the number of small independent retailers due to the squeezing of industry profit margins.¹⁹⁶ In the face of such significant competition from supermarkets, the retail networks of the two largest suppliers, Shell and Esso, had also declined significantly.¹⁹⁷ The OFT therefore found that supermarket growth had “*fundamentally changed the market place*”, however it concluded that the market was competitive overall.¹⁹⁸ It had failed to establish that UK petrol prices reflected either predatory or collusive behavior by any suppliers or retailers and concluded that provided competition between supermarkets and oil companies continued competition

¹⁸⁹ Chapter 2, p47

¹⁹⁰ Chapter 4, p116

¹⁹¹ Office of Fair Trading, *Competition in the supply of petrol in the UK* (OFT 230, 1998) at para 1.16, p8

¹⁹² Ibid at para 1.16, p8

¹⁹³ Ibid at para 14.3, p93

¹⁹⁴ Ibid at para 14.3, p93

¹⁹⁵ Ibid at p3

¹⁹⁶ Ibid at p3 and para 1.16, p8

¹⁹⁷ Ibid at para 1.3, p5

¹⁹⁸ Ibid at para 1.16, p8

was unlikely to suffer.¹⁹⁹ Overall, the OFT established that the diversity of suppliers in the market would make collusive behaviour difficult at both the retail and wholesale level.²⁰⁰ The market was therefore operating competitively and did not require any intervention at that time, despite the reduction in the number of independent retailers in operation.²⁰¹ The OFT did not consider their decline to have significantly weakened competition, as the market was now increasingly supplied by supermarket and company owned sites.²⁰² While independent dealers generally acted as agents for branded suppliers who constrained their scope to adjust prices, supermarkets set their own prices.²⁰³ Consequently, as independent retailers did not offer any benefits for competition beyond those offered by a company or supermarket owned site, their decline was not a concern from a competition perspective.²⁰⁴ The OFT also stated that whilst there had been some entry and exit from the market the number of wholesalers in the UK had not fallen since 1990 and so market foreclosure due to vertical integration from refining to retailing was not a current problem.²⁰⁵ It was however concluded that the market would again require to be monitored to ensure that competition between the major players was not dampened in the event it became more concentrated.²⁰⁶

5. On-going challenges

5.1 Pricing issues in the distribution of beer

Despite the OFT's declarations of competitiveness, both markets have continued to be investigated by the UK competition authorities however both have continued to be cleared of any anti-competitive conduct. As discussed in Chapter 4, amidst claims by the Business Innovation and Skills Committee that the market conditions prior to the Beer Orders were still evident in the UK beer market, the pressure group the Campaign for Real Ale (CAMRA) asserted that the retail on-trade price of beer in 2008 was approximately 3.3-3.5 times more than the price charged in the off-trade, with pubcos' inflated retail prices generally being followed by the market.²⁰⁷ As pubcos were able to increase retail prices above market levels, CAMRA considered this to contribute to the closure of public houses

¹⁹⁹ Ibid at para 1.17, p8.

²⁰⁰ Ibid at para 1.18, p8

²⁰¹ Ibid at para 1.19, p8

²⁰² Ibid at para 14.28-14.29, p98 and 14.36-14.37, p100

²⁰³ Ibid at para 14.30, p98

²⁰⁴ Ibid at para 14.36, p100

²⁰⁵ Ibid at para 14.37, p100

²⁰⁶ Ibid at para 1.19, p8

²⁰⁷ Chapter 4, p123

in the UK.²⁰⁸ The OFT however continued to decline to alter its position that ‘there was no significant competition problem in respect of the beer and pub market’.²⁰⁹ As discussed in Chapter 4 however, as part of the on-going scrutiny of the operation of the beer tie in the UK market, CAMRA submitted a super-complaint to the OFT on the basis that the UK pub industry and the beer tie in particular, are anti-competitive.²¹⁰ As noted in Chapter 4, in dealing with such concerns over the operation of the tie, the OFT has frequently deferred to the fact that they, along with the Competition Commission and the European Commission, have reviewed this and that no new evidence had been presented to justify revisiting it. Further, as discussed in Chapter 4, on rejecting the super complaint the OFT highlighted the large number of competing public houses owned by different operators, and the fact that consumers benefit from competition and choice between these.²¹¹ The fragmented nature of the market was deemed not to facilitate coordinated behaviour and so prohibited pubcos from inflating prices above a competitive level. Again, higher retail prices were attributed to higher costs at the retail level as well as the amenities offered by public houses to their customers, not to a lack of effective competition between them.²¹² The OFT defaulted to the position that consumers benefit from ‘considerable competition and choice’ between public houses, finding no evidence of competition problems significantly impacting on consumers.²¹³ A similar outcome was also reached when the OFT failed to establish any evidence of anticompetitive practices when addressing pricing issues in the distribution of petrol.

5.2 Pricing issues in the distribution of petrol

Whilst pricing concerns in the distribution of beer have focused on increasing retail prices, with regard to the distribution of petrol in the UK numerous investigations have been conducted into the price differential between mainland and rural pump prices, and between different regions and towns. The Highlands and Islands have been highlighted as an area of concern.²¹⁴ The OFT has however established that the increased price differential between this area and urban UK is not necessarily a result of exploitative behaviour, it being noted that competition driven by supermarket forecourts is largely absent in the Highlands and

²⁰⁸ Chapter 4, p127

²⁰⁹ See Chapter 4

²¹⁰ Chapter 4, p126

²¹¹ Chapter 4, p131

²¹² Chapter 4, p131

²¹³ See Chapter 4, p133

²¹⁴ Almost all outlets in these areas were independently owned and subject to 5-year solus agreements. Office of Fair Trading, *Petrol and Diesel Pricing in the Highlands and Islands* (OFT 305, 2000) at para 3.7, p5 and para 3.10, p6) Esso and BP together accounted for between 65% and 90% of supply in the area (ibid at para 3.9, p5).

Islands, although some sites were found to have natural monopoly characteristics.²¹⁵ The OFT failed to establish evidence of excessive profits and whilst retail margins were higher than those in the rest of the UK,²¹⁶ higher retail prices were attributed to, amongst others, higher transportation costs for lower volumes of fuel and the reduced level of business over which fixed costs could be recovered.²¹⁷ Consequently a higher retail margin was deemed necessary if smaller retailers were to remain in business.²¹⁸ The use of ‘fuel’ cards was also highlighted as a potentially contributing factor to the higher prices in these areas as they permitted customers to buy fuel in these rural areas at a national average price.²¹⁹ Consequently, overall the OFT did not consider there to be any general problems of excessive profits or prices.²²⁰ Even in areas deemed worthy of further investigation, such as the Western Isles,²²¹ the OFT again highlighted the absence of a supermarket and established that the total margin earned following deduction of transportation costs, was not much greater than that earned on the mainland prior to the entry of a supermarket.²²² The OFT therefore failed to establish an infringement of the UK competition provisions by local suppliers.²²³ This reliance on the absence of a supermarket as explanation for the widening price differential between urban and rural areas of the UK continued when the OFT revisited the issue in 2012.²²⁴

6. Continued discontentment over the operation of both sectors

Despite the OFT’s failure to establish any problems of excessive profits or pricing in rural areas, the general issue of pricing and the role of supermarkets in particular, has been a recurring one in the UK petroleum market. This was recently addressed in the OFT’s Call for Information in 2012²²⁵ in response to claims that, despite the on-going declarations of competitiveness, the market was not working as well as it should be. This served to highlight the general competitive implications arising from supermarkets’ growing

²¹⁵ Office of Fair Trading, *Petrol and Diesel Pricing in the Highlands and Islands* (OFT 305, 2000) at para 4.13, p12

²¹⁶ Ibid at para 1.3, p1

²¹⁷ Ibid at para 6.1-6.2, p21

²¹⁸ Ibid at para 1.3, p1

²¹⁹ These were offered by all three oil majors, so that business users buying petrol throughout the country benefitted from their use. However, many cards were sold to customers not meeting that profile (ibid at para 5.23-5.24, p18). BP was the largest wholesale supplier in the area and the information available did not permit any firm conclusions as to whether BP had benefitted from their use (ibid at para 5.31, p20).

²²⁰ Ibid at para 6.2-6.3, p21

²²¹ Ibid at para 6.3-6.4, p21

²²² Office of Fair Trading, *Competition Act 1998 The retail market for petrol and diesel in Lewis and Harris* (12th October 2001) at para 28

²²³ Ibid at para 30

²²⁴ Office of Fair Trading, *Petrol and Diesel Pricing in the Scottish Islands* (OFT 1432, 2012) at para 1.12,

p7

²²⁵ Above, n.17

participation in the distribution of fuel with some parallels being evident with the concerns discussed in Chapter 5 regarding the role of supermarkets in the distribution of beer in Australia. However, around about this time, similar discontentment over the operation of the beer tie prompted it to again be revisited by the UK Government, this time resulting in a statutory code for pubcos, although this was not a response to anticompetitive behaviour within the sector.

6.1 The Small Business, Enterprise and Employment Act 2015

As discussed in Chapter 4, numerous reports have long urged the Government to take action in addressing the competitive implications associated with the operation of the beer tie. However, as already mentioned it has long deferred to the OFT's finding that there is no evidence of competition problems having an adverse impact on consumers and it has also been reluctant to intervene in the negotiation of the terms of commercial contractual relationships.²²⁶ Following the OFT, the Government has also highlighted that the beer tie is accepted as a legitimate business model under EU law and the apparent absence of any competition issues that significantly affect consumers, as justification for their restraint in intervening.²²⁷ Nevertheless, in 2013 the Government was finally persuaded of the need for a statutory code of conduct to regulate the relationship between pubcos and their tied tenants.²²⁸ The Government did not intend to include a mandatory free-of-tie option in the Code given the potential implications of such an obligation, its aim being simply to ensure that tied tenants are treated fairly and are no worse off than their free-of-tie counterparts.²²⁹ Consequently the Code was not intended to be a departure from the position that there are no competitive problems having an impact on consumers. However, in contrast to the petrol market, given MP intervention in the Small Business, Enterprise and Employment Bill 2014, which received Royal Assent in March 2015 and includes a Market Rent Only (MRO) option, as noted in Chapter 4, the UK beer market is now faced with its most significant intervention since the notorious Beer Orders of 1989, even although the UK Government has not departed from its position that the market is operating competitively.

²²⁶ Chapter 4, p135

²²⁷ Chapter 4, p135

²²⁸ Chapter 4, p 137

²²⁹ Chapter 4, p138-139

6.2 Increasing focus on the role of supermarkets in the distribution of petrol

Around about the time the Government revisited the issue of the beer tie, in 2012 a call for information was launched in response to claims, mainly by the Petrol Retailers Association,²³⁰ that the UK petrol sector was not working as well as it should, with the aim being to determine how best to rectify any competition issues.²³¹ By contrast to the brewing industry where the concerns remained pubcos' operation of the tie, the primary concern in the distribution of petrol was now the rise and influence exerted by supermarkets, with broad parallels being evident with their role in the distribution of beer in Australia, as discussed in Chapter 5.²³² Included amongst the issues addressed by the OFT was that of local competition and the influence of supermarkets; independent retailers ability to compete fairly with supermarkets and oil company owned sites; and the issues of rocket and feather pricing,²³³ although it would ultimately conclude that competition is working "*relatively effectively*".²³⁴ At the outset it was noted that the price of petrol is influenced by factors including taxation and crude oil prices, and in contrast to pubcos which have ultimately driven up the retail price of beer, petrol price increases over the past decade have not been significantly influenced by increased margins earned by refiners, wholesalers or retailers.²³⁵ Before tax and duty, the UK has amongst the cheapest petrol prices in Europe although after tax and duty these increase to amongst the highest.²³⁶ Consequently, the OFT opted not to pursue these increasing prices at a national level.²³⁷ The issue of varying pump prices between neighbouring towns and in rural areas was also acknowledged and subsequently dismissed by the OFT, although they did not rule out the possibility of taking action at a local level in the future should evidence be presented to merit this.²³⁸

²³⁰ The Association represents independent fuel retailers and forecourts in the UK and Northern Ireland. ('About the PRA' (*Petrol Retailers Association*) <<http://www.rmif.co.uk/associations/pr/about-the-pra/about/>> accessed 20th April 2015)

²³¹ Above, n.17 at para 1.2, p4

²³² Chapter 5, p196

²³³ Above, n.17 at para 1.3, p4. 'Rocket and feather pricing' occurs when pump prices are raised quickly in response to increases in crude oil prices and lowered slowly in response to reductions. This can indicate a lack of effective competition between suppliers (ibid at para 6.1 and 6.3, p106.) There was insufficient evidence to support this in the UK market (ibid at para 6.41, p122.)

²³⁴ Above, n.17 at para 1.4, p4

²³⁵ Ibid at para 1.23, p13

²³⁶ Ibid at para 1.5, p5

²³⁷ Ibid at para 1.23, p13-14

²³⁸ Ibid at para 1.26, p14

6.2.1 Supermarkets and their influence on local competition

The OFT addressed concerns over local competition and varying pump prices.²³⁹ Whilst acknowledging their existence, the OFT sought to rely on a number of possible explanations for differing prices including cost factors such as transportation of fuel, as well as local competition between wholesalers and retailers.²⁴⁰ As the OFT considered wholesale competition to be ‘reasonably effective’ it was deemed unlikely that variations in wholesale competition significantly impact on pump prices except in rural areas with fewer wholesale suppliers.²⁴¹ Considering local competition, the most important factors were noted as the number of local competitors, and the number of supermarkets present.²⁴² With regard to higher prices in rural areas the OFT once more deferred to the reduced volumes sold by forecourts in these areas, increased costs of supply, and fewer supermarkets as an explanation for this.²⁴³ With regard to supermarkets, the OFT noted the increased market share now held by them with the big four supermarkets’ market share of road fuel sold in the UK having increased by 10% between 2004 and 2012, to 39%.²⁴⁴ This growth was however considered a positive development from the consumer’s perspective. Their countervailing buyer power enabled them to buy wholesale road fuels at lower prices than other retailers, and the large volumes sold enabled them, to operate on lower margins and to offer consumers lower prices than elsewhere.²⁴⁵ The OFT found that this pressurised independent retailers and oil companies to follow suit and reduce their prices, although many retailers have ultimately found it very difficult to do so.²⁴⁶ As a result, similarly to the number of public houses in operation in the UK, the number of forecourts has continued to decline.²⁴⁷ The OFT, however, similarly to its finding that consumers benefit from significant competition and choice between public houses, found that in areas of closures, retail competition was still strong.²⁴⁸

²³⁹ Ibid at para 1.13, p10

²⁴⁰ Ibid at para 4.50, p86

²⁴¹ Ibid at para 4.17, p68

²⁴² More specifically, they highlighted the operation of an Asda store, due to their aim of offering the lowest fuel price in an area (ibid at para 4.4, p59.)

²⁴³ Ibid at para 1.13, p10-11. Higher prices at motorway sites were also considered. The OFT was satisfied that their operating costs were higher than other forecourts, requiring higher retail prices, even though they sold higher fuel volumes than other forecourts (ibid at para 4.46, p83-83). Proposals were made to increase the transparency of prices at these sites (ibid at para 4.49, p86).

²⁴⁴ Ibid at para 1.9, p9

²⁴⁵ Ibid at para 1.9, p9

²⁴⁶ Ibid at para 1.9-1.10, p9

²⁴⁷ Ibid at para 1.10, p9

²⁴⁸ Ibid at para 1.10, p9

6.2.2 Independent retailers unable to compete fairly with supermarket and oil company-owned sites

Whilst the rise of the supermarket forecourt has generally been perceived as a positive development from the consumer's perspective due to their ability to lower retail prices, the OFT was also forced to consider independent dealers' ability to compete fairly in the retail sector, given their submissions highlighting supermarket and oil company practices that made this difficult.²⁴⁹ The OFT noted the on-going decline in the number of independent retailers over the past 10 years, and considered some of the challenges facing them.²⁵⁰ They found that independent retailers generally have to pay a higher wholesale price for fuel compared to supermarkets.²⁵¹ The OFT did not, however, consider this to be surprising due to their limited bargaining power.²⁵² They noted that supermarkets' bargaining power enabled them to draw on a wide range of suppliers and as they were not limited to a particular branded wholesaler they were able to negotiate lower wholesale prices.²⁵³ Due to the significant levels of business supermarkets offer wholesalers they also generally enjoyed preferential supply terms, with this ultimately benefitting consumers through the lower retail prices charged.²⁵⁴ However, as already mentioned it was accepted that there may be some issues at the local level. Concerns over the operation of forecourts in certain rural areas had prompted initiatives such as the Rural Petrol Stations Grant Scheme, which was introduced in an attempt to assist rural petrol stations particularly vulnerable to closure.²⁵⁵ The OFT did not however consider there to be sufficient evidence of practices against independent dealers that would justify investigating the matter further.²⁵⁶

²⁴⁹ Ibid at para 1.15, p11. Their concerns included independent dealers' lack of bargaining power when purchasing wholesale fuels; supermarkets charging low or below cost pump prices; oil company-owned sites selling fuel close to or below the wholesale price charged to independent dealers; and the limited choice of wholesaler suppliers available to independent retailers when purchasing fuels wholesale (ibid at para 5.2, p88).

²⁵⁰ Ibid at para 5.33, p105

²⁵¹ Ibid at para 5.4, p88-89

²⁵² Ibid at para 5.4, p88-89

²⁵³ Ibid at para 5.4, p88-89

²⁵⁴ Ibid at para 5.4, p88-89

²⁵⁵ This aims to assist in the maintenance of essential services in rural communities (*Review of rural petrol stations grant scheme Final Report* (The Scottish Government, 30th August 2004) <<http://www.scotland.gov.uk/Publications/2004/08/19629/40004>> accessed 21st April 2015). In 2009, grants were made in Aberdeenshire ('Lifeline for rural petrol stations in Aberdeenshire' (The Scottish Government, 31st March 2009) <<http://www.scotland.gov.uk/News/Releases/2009/03/31163821>> accessed 3rd July 2015).

²⁵⁶ Above, n.17 at para 1.12, p6

6.2.3 Supermarkets pricing below wholesale level and engaging in predatory practices

Whilst concerns in the distribution of beer in the UK are still focused on increasing retail prices, the OFT considered and rejected concerns that supermarkets were charging fuel prices close to, or below, the wholesale level as they were able to cross-subsidise this with profits earned through their grocery business.²⁵⁷ The Chairman of the Petrol Retailers' Association claimed that fuel discounts offered by supermarkets lead to higher grocery prices and caused the closure of small independent retailers faced with aggressive competition from supermarkets.²⁵⁸ They therefore argued that the OFT should have proposed similar action to that taken in Australia where supermarkets are no longer allowed to offer fuel discounts which are funded by other parts of their business, namely groceries and are limited to fuel saving offers that do not exceed 4 cents per litre.²⁵⁹ Nevertheless, supermarkets submitted to the OFT that they operated as stand-alone businesses, and the OFT identified evidence to support this including that their lower prices were due to their increased bargaining power and larger volumes of fuel sold.²⁶⁰ The OFT also dismissed claims by independent retailers that supermarket fuel promotions might ultimately amount to selling fuel below cost.²⁶¹ Independent retailers claimed these promotions were only possible as grocery prices were inflated to subsidise lower fuel charges, to the disadvantage of those customers who only purchased groceries at the supermarkets in question.²⁶² This was however dismissed on the basis that the groceries market is competitive and consumers have a significant choice of retailers to buy groceries from should prices be inflated.²⁶³ The OFT also dismissed the possibility that supermarkets were engaging in predatory behavior against independent dealers.²⁶⁴ It noted that rival supermarkets and oil companies offered lower prices than independent retailers and would remain in the market after an independent retailer exited.²⁶⁵ Subsequently they would

²⁵⁷ Ibid at para 5.7, p91. No supermarket held a dominant position in a relevant market, as required for below cost selling of road fuel to be prohibited by the Chapter II prohibition of the Competition Act 1998. It accepted the possibility of dominance in local areas (ibid at para 5.16, p94-95).

²⁵⁸ Retail Motor Industry Federation, 'Supermarket fuel discount should face Axe says PRA' (*Retail Motor Industry Federation*, 25th February 2013), <<http://www.rmif.co.uk/press-room/press-releases/supermarket-fuel-discounts-should-face-axe-says-pra-25-02-13/?y=2013&m=2>> accessed 3rd July 2015

²⁵⁹ 'Coles and Woolworths undertake to cease supermarket subsidised fuel discounts' (*Australian Competition and Consumer Commission*, 6th December, 2013) <<http://www.accc.gov.au/media-release/coles-and-woolworths-undertake-to-cease-supermarket-subsidised-fuel-discounts>> accessed 3rd July 2015 and above, n.258

²⁶⁰ Above, n.17 at para 5.8, p91

²⁶¹ Ibid at para 5.10, p92 and para 5.16, p94-95

²⁶² Ibid at footnote 134, p92

²⁶³ Ibid at footnote 134, p92

²⁶⁴ Ibid at para 5.14, p93-94

²⁶⁵ Ibid at para 5.14, p93-94

prevent supermarkets recouping losses resulting from their predatory strategy.²⁶⁶ Further, it was noted that there did not appear to be significant barriers to entry to the retail market. A number of new sites opened, and several closed sites had re-opened,²⁶⁷ although independent dealers claimed that supermarkets benefitted from favourable planning terms when opening new sites.²⁶⁸ Nevertheless, in light of the lack of examples of supermarkets causing the exit of independent dealers due to predatory behaviour, and the lack of evidence that consumers were suffering reduced choice and higher costs in areas where independent retailers had exited, the OFT considered that it lacked the necessary evidence to investigate this further.²⁶⁹

6.2.4 Reduced competition in the wholesale sector - not a problem shared

Similarly to concerns discussed in Chapter 4 over the lack of wholesale competition in the supply of beer, independent petrol retailers also complained that there was a lack of competition in the petrol wholesale sector, highlighting the decline in the number of branded wholesale options open to them.²⁷⁰ They claimed that their limited avenues of supply meant they had very limited room to negotiate their supply contracts with wholesalers.²⁷¹ This was more so for independent retailers dealing in a single brand of fuel than supermarkets, which are unrestricted in their choice of supplier. Further, changes in the source of supply are very costly due to, amongst others, the cost of rebranding forecourts.²⁷² Independent dealers also alleged that branded suppliers tended to make unattractive offers of supply as they wished to focus on expanding their own supply networks and tended to shun smaller sites with low throughputs.²⁷³ Nevertheless, the OFT relied on evidence that the wholesale market had benefitted from importers and blenders increasing their market share due to supermarkets purchasing unbranded fuel from a range of sources.²⁷⁴ Whilst they concluded that overall the UK wholesale sector is competitive, they did however acknowledge that there are areas of the country, such as Scotland, where wholesale competition is weaker, with only limited branded supply options available.²⁷⁵ Concerns over anticompetitive behavior prompted an investigation into the supply of fuel

²⁶⁶ Ibid at para 5.14, p93-94

²⁶⁷ Ibid at para 5.14, p93-94

²⁶⁸ Ibid at para 5.29, p103

²⁶⁹ Ibid at para 5.15, p94

²⁷⁰ They claimed these had declined since the OFT'S 1998 Report (ibid at para 5.22, p97).

²⁷¹ Ibid at para 5.22, p97

²⁷² Ibid at para 5.24, p97-98

²⁷³ Ibid at para 5.22, p97 and para 5.25, p98

²⁷⁴ Ibid at para 1.11, p10

²⁷⁵ Ibid at para 5.26, p98 and para 5.27, p99

in the Western Isles of Scotland, with the OFT also undertaking to investigate complaints as they arise.²⁷⁶

6.2.5 Competition still working effectively

Despite the numerous concerns raised, most notably those of independent retailers facing aggressive competition from supermarket forecourts, the OFT again concluded that competition in the UK road fuel sector is working relatively effectively.²⁷⁷ None of the practices by retailers or wholesalers were found to amount to a breach of the Competition Act 1998²⁷⁸ and the OFT Chief Executive supported this finding by stating that while they “...recognise that there has been widespread mistrust in how this market is operating...our call for information has not identified any evidence of anticompetitive behavior in the fuel market at a national level, where competition appears to be strong.”²⁷⁹ However he did acknowledge that there may be some competition issues at a more local level and that action may be taken where evidence is provided.²⁸⁰

While the OFT found that competition in the sector is working relatively well, there were claims that the OFT had ‘turned their back’ on one of the primary issues, namely fuel discounting.²⁸¹ At a time when as mentioned above Australia’s largest supermarkets, Coles and Woolworths, had recently undertaken not to offer customers discounted petrol subsidised by their grocery business, the Petrol Retailers Association claimed it was ‘imperative’ that the OFT re-open their investigation.²⁸² The Australian Competition and Consumer Commission reached agreement with the two biggest supermarkets that they would stop offering discounts following its finding that this was resulting in a substantial

²⁷⁶ In January 2013 the OFT, now the Competition and Markets Authority (‘CMA’), launched an investigation into the distribution of road fuel in the Western Isles. Most filling stations there were tied to Certas Energy UK Limited to buy fuel exclusively for 5 years. Following the CMA investigation, commitments were given to bring these contracts to an end, providing forecourts with greater flexibility to choose where to source their fuel. (‘CMA accepts commitments to improve access to road fuels market in the Western Isles’ (*Competition and Markets Authority*, 24 June 2014)

<<https://www.gov.uk/government/news/cma-accepts-commitments-to-improve-access-to-road-fuels-market-in-the-western-isles>> accessed 3rd July 2015 and ‘Distribution of road fuels in parts of Scotland’ (*Competition and Markets Authority*, 12th August 2014) <<https://www.gov.uk/cma-cases/investigation-into-the-distribution-of-road-fuels-in-parts-of-scotland>> accessed 3rd July 2015)

²⁷⁷ Above, n.17 at para 1.4, p4

²⁷⁸ The OFT had insufficient evidence to investigate whether any supermarkets or wholesalers had, or had abused, a dominant position under Chapter II of the Competition Act 1998 (ibid at para 5.34, p105).

²⁷⁹ ‘OFT points to competition working well in UK road fuel sector’ (*Wiredgov*, 31st January 2013) <<http://www.wired-gov.net/wg/wg-news-1.nsf/0/D3DE148299719A6080257B04004F28E1?OpenDocument>> accessed 3rd July 2015

²⁸⁰ Ibid

²⁸¹ Above, n.258

²⁸² ‘PRA Call for subsidised fuel discounting to cease in UK’ (*Petrol Retailers Association*, 12th December 2013) <<http://www.rmif.co.uk/press-room/press-releases/pr-a-call-for-subsidised-fuel-discounting-to- cease-in-uk-12-12-13/?y=2013&m=12>> accessed 3rd July 2015

lessening of competition in the medium to long term.²⁸³ The Petrol Retailers Association subsequently claimed that this discredited the OFT's response to the concerns raised regarding unfair competition in the UK fuel market.²⁸⁴ Similarly to the UK, where, as discussed above, forecourt closures are continuing due to aggressive pricing and discounting by supermarkets, the Australian competition authorities were concerned by the long term effects of supermarkets deep discounting on the structure of the retail fuel market.²⁸⁵ Essentially this was a lack of choice and higher prices, as competition is removed from the market.²⁸⁶ Subsequently, in light of the Petrol Retailers Association's plans to continue to lobby the UK competition authorities to re-open their investigation, with the intention of achieving similar agreement with the UK's big four supermarkets,²⁸⁷ it is most likely that this sector, similarly to the brewing industry, will once again be under investigation.

7. No anticompetitive declarations in either sector

With the exception of the Beer Orders and now the 2015 Act, despite the numerous and on-going investigations and concerns over the retail distribution of beer and petrol in the UK, reflecting the general mistrust in the operation of these markets, the UK competition authorities have been unable to identify any anti-competitive conduct within either market. From the foregoing review of these, various reasons appear to have been provided in explanation of this. In the distribution of beer, the OFT has generally refused to attribute increasing retail prices to a failure in retail competition. As already mentioned, it has instead resorted to the position that retail competition is manifest in the increased level of amenity and service provision with consumers benefitting from greater choice of amenity and price combinations.²⁸⁸ Consequently, increased retail prices have been attributed to the 'package of features' offered by public houses, not a lack of retail competition between them.²⁸⁹ In rejecting concerns that pubco ownership of public houses has enabled them to inflate prices above a competitive level and notwithstanding the continuing decline in public houses, as mentioned above, the OFT has highlighted the large number of pubs owned by different operators, and the fact that they consider consumers benefit from competition and choice between these. This fragmentation within the market has been deemed to prohibit coordinated behaviour. With regard to competition at the wholesale

²⁸³ Ibid

²⁸⁴ Ibid

²⁸⁵ Ibid

²⁸⁶ Ibid

²⁸⁷ These are Tesco, Asda, Sainsbury's and Morrisons (ibid).

²⁸⁸ See Chapter 2, p44

²⁸⁹ See Chapter 4, p131

level, whilst a diverse and independent wholesale sector has failed to materialise in the distribution of beer, with this still being dominated by the largest brewers, and being a source of concern in the numerous reports produced on the market, the OFT has generally deferred to the improved market entry at the retail level, which it considers to be increasingly differentiated.²⁹⁰

The OFT also appears to have been similarly optimistic when addressing competition concerns in the distribution of petrol. As noted above, reliance has been placed on market entry and exit at the wholesale level and the general maintenance of diversity of suppliers at that level in ensuring foreclosure due to vertical integration from refining to retailing is not a problem. At the retail level, when considering the possibility of predatory practices by supermarkets, the OFT has generally been satisfied that so long as competition between oil companies and supermarkets continues, competition will not suffer, even if the number of independent dealer owned sites continues to decline. Further, in addressing increasing pump prices in rural areas, the OFT has repeatedly deferred to the reduced volumes sold by the forecourts in these areas, increased costs of supply, and the absence or reduced number of supermarkets, as an explanation for this. Levels of local competition have been used to explain retail price differences between neighbouring towns and regions. Although the authorities remain open to the possibility of anticompetitive practices at the local level, similarly to the distribution of beer, there has still been no acceptance of any anticompetitive practices at a national level, despite campaigning by pressure groups.

Whilst these continuing declarations of competitiveness in the face of significant and on-going discontent are just one of the many shared similarities in the distribution of beer and petrol, there are certain features that distinguish them from each other and require some consideration in order to determine whether any guidance can be gleaned from the distribution of petrol in reforming the distribution of beer in the UK.

8. Distinguishing features in the supply of beer and petrol

Despite the many similarities between the brewing and petrol industries, there are certain features distinguishing them from each other. Therefore, in order to determine what guidance can be gleaned from the retail distribution of petrol in reforming the distribution of beer in the UK, regard will be had to these here. In doing so, focus shall be placed on the heterogeneous nature of beer compared with petrol's homogeneous qualities. In light of this it will be shown that issues connected to restrictions on consumer choice that have

²⁹⁰ Chapter 2, p44

been prevalent in relation to the operation of the beer tie, have not been of concern in the distribution of petrol. It will also be highlighted that beer, unlike petrol, has two main and directly competing avenues of distribution to the final consumer, as opposed to one in the distribution of petrol. This second avenue of distribution, namely the off-trade, is similar to the UK petrol distribution market as it is increasingly dominated by supermarkets.

8.1 Heterogeneous v. homogenous

As already mentioned in Chapter 3, beer is a heterogeneous product, whilst petrol is homogeneous.²⁹¹ The production processes, raw materials and recipes used in the production of beer are differentiated, resulting in varying tastes and appearances.²⁹² As a result, strong brand loyalty, regional preferences for locally brewed beer, and increased demand for craft beers due to their unique production techniques and flavours, are all factors affecting the industry and are not reflected in the distribution of petrol. Consequently, certain concerns raised regarding the distribution of beer, have not been reflected in the UK competition authorities investigations into the supply of petrol. As discussed in Chapters 2 and 4, restrictions on consumer choice have been an inevitable, but highly problematic, aspect of the widespread use of the beer tie. Whilst petrol was once considered to be a heterogeneous product, with major producers relying heavily on branding to differentiate their products, since the introduction in 1971 of legislation requiring petrol be sold by the ‘star’ octane grading, petrol, grade for grade has essentially been regarded as a homogenous product in the eyes of consumers.²⁹³ Consequently, even although, on account of the significant costs and logistical constraints involved, petrol stations can only sell one brand of fuel, this has not prompted concerns over restrictions on consumer choice. From the foregoing review it is apparent that this limitation has only proven problematic to branded retailers. As already noted, this is due to the fact they are reliant upon branded suppliers, and so are restricted when negotiating the terms of their supply contract, should they wish to avoid the expense of switching supplier. However, a further consequence of petrol being homogeneous as opposed to heterogeneous, again distinguishing it from beer, is that price and convenience are now the principal driving factors in the consumer’s choice of petrol forecourt.²⁹⁴ These factors have facilitated the growth in supermarkets’ market share as they are able to offer fuel at reduced prices whilst

²⁹¹ Chapter 3, p66

²⁹² W.J. Adams, ‘Determinants of the concentration in beer markets in Germany and the United States: 1950-2005’ in J.F.M Swinnen, ed, *The Economics of Beer* (New York, Oxford University Press Inc, 2011) at p229 and M Jackson, *Ultimate Beer* (New York, DK Publishing, 1998)

²⁹³ Above, n.140 at para 43, p20

²⁹⁴ Above, n.17 at para 4.23, p72

also offering increased services, thereby attracting customers to their forecourts. By contrast, brand loyalty is still a feature of the beer market, and whilst low prices and services offered by public houses are influential in consumer choices, they are not the only factors informing their choice of public house. Nevertheless, beyond these differences in the nature of the products involved, and the factors influencing consumer choices in each market, the distribution of beer is also distinguishable from petrol on account of the fact that it has two main avenues of distribution to the final consumer.

8.2 Two avenues of distribution– the on and off-trade for beer

Unlike petrol, which is retailed to consumers through petrol forecourts, beer has two main, directly competing, avenues of distribution to the final consumer. As mentioned in Chapter 2, in addition to the on-trade, which involves the distribution of beer for consumption in the premises in which it is sold, such as public houses; beer is also sold to the final consumer via off-trade outlets, namely those licensed to sell alcohol for consumption off of the premises.²⁹⁵ Today, the off-trade sector is comprised of multiple retailers, such as supermarkets or convenience stores; and specialised alcohol retailers, namely off-licenses.²⁹⁶ This off-trade has no equivalent in the supply of petrol. However, similarly to the distribution of petrol, this distribution channel is increasingly dominated by the UK's largest supermarkets, with this also being the case in the distribution of beer in the US, Australia and increasingly in Belgium, as discussed in Chapter 5. Whilst the on-trade, namely public houses, has traditionally dominated the supply of beer in the UK, the relatively recent downturn in economic conditions has prompted increased demand for comparatively cheaper off-trade beers.²⁹⁷ Given this demand for low alcohol prices, supermarkets have rapidly gained market share in the UK off-trade. Similarly to supermarket involvement in the distribution of petrol, one of the primary trends in the UK off-trade has been supermarkets' offering beer at greatly reduced retail prices compared to other off-trade outlets.²⁹⁸ This has also been a trend in the other geographic markets considered in Chapter 5. Consequently, similarly to other national markets, as well as the UK petroleum market, supermarkets now also have a prominent role in the off-trade distribution of beer in the UK. Therefore, notwithstanding the fact that supermarkets have managed to evade any conclusions that they are engaging in anticompetitive practices in the distribution of fuel in the UK, their increasingly prominent role is one of the primary observations gleaned from this review of it. Further, in light of the fact that the on and off

²⁹⁵ K Hughes, (ed), 'Market Report 2014, Take-Home Trade' (Key Note) at p2

²⁹⁶ Ibid at p2

²⁹⁷ Ibid at p2

²⁹⁸ Ibid at p3

trade for beer in the UK are in direct competition, and given that proposals to rebalance the beer tie which is widely used in the on-trade will most likely result in increased beer sales via the off-trade, as has been the case in Australia, the increasingly significant role of supermarkets may merit further consideration.

9. The rise and influence of supermarkets in the distribution of beer

From the foregoing review of the distribution of petrol which, notwithstanding the differences identified, generally shares many similarities with the distribution of beer, it is evident that there has been a shift away from competition concerns focused on the level of vertical integration in distribution, to the increasingly dominant role of supermarkets and their associated implications. However, this increasing participation by supermarkets is also reflected not only in the UK off-trade for beer, but is an increasingly global trend as highlighted in the review of the US, Australian and Belgian beer markets considered in Chapter 5.

9.1 Global trend – increased off-trade sales via supermarkets

As discussed in Chapter 5, following the general outlawing of the beer tie in Australia as an illegitimate business model, the off-trade is now the primary means of distributing beer to the final consumer and is dominated by supermarket chains Coles and Woolworths. However, similarly to supermarket participation in the distribution of petrol in the UK, this increased role of supermarkets has attracted the attention of the competition authorities. Concerns over, amongst others, the imbalanced bargaining power between supermarkets and suppliers generally have caused the Australian competition authorities to consider this issue, with some politicians calling for legislation to instigate divestiture in the supermarket sector.²⁹⁹ However, this trend of increased off-trade beer sales through supermarkets is also evident in the US and Belgium, which as discussed in Chapter 5 accepts the beer tie as a legitimate business model, similarly to the UK and also has one of the most diversified beer markets in the World. Today, the majority of Belgian beer sales are through the off-trade, with supermarkets accounting for the largest share of the market.³⁰⁰ Nevertheless, the Belgian on-trade sector is still considered to be strong and in contrast to the UK market has a reasonably large wholesale and distribution sector supplying it.³⁰¹ Consequently, the increasing influence of supermarkets has had different

²⁹⁹ See Chapter 5 at p 197

³⁰⁰ See Chapter 5, p 214

³⁰¹ See Chapter 5, p214

effects in the jurisdictions considered in Chapter 5, however the UK experience would appear to be more aligned with the Australian example.

9.2 Supermarket domination of UK off-trade

Supermarkets have been licensed to sell beer in the UK since the 1960s,³⁰² and as mentioned above following the recent economic downturn, the off-trade sector in general has benefitted from significant growth in sales due to their comparatively cheaper alcohol prices over the on-trade. However, whilst enjoying steady growth, the market has also undergone significant structural changes over the past ten years, due to a substantial decline in one of the traditional distribution avenues, namely the off-license. As a result, many national operators have largely or completely disappeared from the high street.³⁰³ This has coincided with the increasingly strong market position enjoyed by supermarkets. Their significant growth has been attributed to their low prices; the convenience of their 'express' store formats, which are now widespread on the UK's high streets; and the general convenience of purchasing groceries and alcohol from the same store, which have all attracted consumers away from traditional off-licenses.³⁰⁴ Consequently, in 2013 it was estimated that multiple grocers, namely supermarkets and convenience stores, now account for 75% of the UK market for take home alcohol by type of retailer by value.³⁰⁵ Only two of the largest national off-licences are still in operation, and given the considerable competition faced by independent off-license stores, it is expected that supermarkets will continue to increase their share of the market.³⁰⁶ Subsequently, similarly to the Australian experience of supermarket involvement in the distribution of beer considered in Chapter 5, as well as the Australian experience of their involvement in the distribution of petrol, given the continued expansion of UK supermarkets and the declining number of major players in the UK off-trade market, today competition within this market is less robust than it has been.³⁰⁷

9.3 Low beer prices

In light of the foregoing, similarly to their involvement in the distribution of petrol in the UK, supermarkets have used their increased purchasing power and economies of scale in

³⁰² J Kneale 'British drinking from the 19th century to present' (*UK Parliament*, April 2009) <<http://www.publications.parliament.uk/pa/cm200910/cmselect/cmhealth/151/151we16.htm>> accessed 3rd July 2015

³⁰³ National operators included Oddbins. Above, n.295 at p1

³⁰⁴ Ibid at p1

³⁰⁵ Ibid at Table 4.1, p20

³⁰⁶ Above, n.295 at p3. The remaining off-licenses have survived by focusing on unique selling points such as specialist product knowledge (ibid at p22).

³⁰⁷ Ibid at p18

the distribution of beer to expand their market share at the expense of the traditional off-license stores.³⁰⁸ A key element of this has been their ability to offer alcohol at very low retail prices with their increased buyer power being influential in the same way as it has been in the offer of cheap petrol to customers.³⁰⁹ By comparison to smaller chains and independent off-licenses, which generally have to go through a wholesale intermediary to obtain supplies, supermarkets tend to be supplied directly by producers.³¹⁰ In a similar fashion to pubcos, which source supplies directly from brewers, breweries are the main suppliers of beer to the off-trade, enabling supermarkets to use their significant buyer power to negotiate their terms of supply. These breweries are mainly the larger brewers such as Heineken, Molson Coors and Carlsberg.³¹¹ Supermarkets have subsequently been able to offer substantially discounted deals on alcohol, often at below cost price, in an attempt to generate increased demand and increase their market share.³¹² These deep discounts have been significant enough for the Government to take measures to tackle this in an attempt to prevent excessive consumption.³¹³ However, despite the UK off-trade being in direct competition with the on-trade, this does not appear to have encouraged pubcos to reduce retail on-trade beer prices, which as discussed above, are continuing to increase and are an on-going issue. Nevertheless, this practice of offering substantial discounts on groceries, including beer, has attracted the attention of the UK competition authorities.

9.4 Competition concerns over supermarket involvement

Similarly to supermarket participation in the distribution of petrol, their role in the grocery market has also prompted investigations by the UK competition authorities. The Competition Commission³¹⁴ in its market investigation into the supply of groceries in 2000 identified two complex monopoly situations.³¹⁵ It considered that the supermarket practice of consistently selling some products below cost distorted competition and damaged

³⁰⁸ Ibid at p21

³⁰⁹ Ibid at p18

³¹⁰ Ibid at p29

³¹¹ Ibid at Table 4.3, p30

³¹² Ibid at p3

³¹³ Ibid at p19

³¹⁴ Now part of the CMA

³¹⁵ It was to determine whether under the Fair Trading Act 1973 a monopoly situation existed in the supply in UK of groceries from multiple stores (Competition Commission, *Supermarkets A report on the supply of groceries from multiple stores in the United Kingdom Volume 1: Summary and Conclusions* (October 2000) at para 1.1, p3). The complex monopoly situations concerned the pricing of groceries and acting to adversely affect the competitiveness of some of their suppliers (ibid at para 2.325, p71).

smaller grocery retailers and convenience stores.³¹⁶ It was also concerned by the behavior of the five largest grocery retailers towards their suppliers, with the Supermarket Code of Practice being introduced to regulate this.³¹⁷ The supply of groceries by retailers was subsequently reviewed again in 2006, and whilst overall the industry was deemed to be effective and delivered good outcomes for consumers, it was concluded that “*not all is well*”.³¹⁸ In addition to their strong positions in local markets presenting a barrier to entry to competing grocery retailers, supermarkets’ relationships with suppliers, which includes brewers, was highlighted as a potential problem.³¹⁹ However, in considering the competition issues in the supply chain, it was noted that the buyer power enjoyed by the largest grocery retailers may be offset by the market power of the suppliers of the most prominent brands, such as the largest brewers.³²⁰ Supermarket buyer power was ultimately deemed to be beneficial for consumers due to the fact that the lower prices resulting from this were ultimately passed on to them in lower retail prices.³²¹ They did not consider supermarkets’ practice of selling below cost to amount to predatory behavior against other retailers and was not likely to result in an adverse effect on competition.³²² They also went further and considered that temporary promotions on products, including fuel, to increase footfall and boost sales may represent effective competition between retailers and may benefit consumers by reducing the cost of their shopping.³²³ The Commission did however once again highlight its concerns over supermarkets’ relationships with suppliers stating that that should they pass on excessive risks or unexpected costs to suppliers, this would reduce the incentives for them to invest in new products and production processes, which would ultimately be to the detriment of consumers.³²⁴ This prompted some tightening of

³¹⁶ Competition Commission, *Supermarkets A report on the supply of groceries from multiple stores in the United Kingdom Volume 1: Summary and Conclusions* (October 2000) at para 1.6(a), p5. There were also concerns over their practice of charging varying prices in different geographical locations (ibid at para 1.6(b), p5). No remedial action was proposed as the market was generally competitive and due to the need to ensure any intervention was proportionate (ibid at para 1.7 and 1.8, p6).

³¹⁷ Ibid at para 1.9-1.10, p6, and para 1.12, p7. The concern was that their practices would reduce the competitiveness of suppliers and so they would be less likely to invest in product development and innovation, ultimately causing a reduction in quality and consumer choice. It would also cause there to be fewer new entrants to the supplier market (ibid at para 1.11, p7).

³¹⁸ The OFT referred the matter to the Competition Commission in 2006, with it reporting in 2008. Competition Commission, *The Supply of Groceries in the UK market investigation* (April 2008) at para 1 and para 2, p6

³¹⁹ Ibid at para 2-3, p6

³²⁰ Ibid at para 35, p11

³²¹ Ibid at para 36, p12.

³²² Ibid at para 19, p9

³²³ Ibid at para 19-20, p9

³²⁴ Ibid at para 36, p12

the terms of Supermarket Code of Practice and the establishment of an Ombudsman to oversee the revised code.³²⁵

10. Conclusion

In light of the foregoing, it is apparent that there are many similarities between the distribution of beer and petrol. Both are scale economies and as such producers within each have long strived to achieve vertical integration and have gone about this in similar fashions. This has primarily been through the ownership of retail outlets and the widespread use of exclusive purchasing agreements. In light of the shared peculiarities of these markets, the exclusive purchasing agreements within them have been singled out for special handling at the EU level, with this being a largely unique approach distinct from that adopted in the other jurisdictions considered in Chapter 5. Whilst this special handling has been influenced by several factors, and was most evident in the terms of Regulation 1984/83, this is still evident today under the terms of Regulation 330/2010. This deference at the EU level towards beer tie and solus agreements has subsequently also filtered through to the UK competition authorities' approach to complaints regarding the practices within the distribution beer and petrol industries.

As has been shown, complaints concerning the operation of both of these sectors have been numerous and on-going over many decades, prompting several investigations by the UK competition authorities. The earliest of these focused on issues common to both sectors, namely the levels of vertical integration and the possible existence of a monopoly situation. However, whilst critical of both, these reports were generally less scathing with regard to the distribution of petrol. This was due to its relatively competitive wholesale sector, which was, and still is, lacking in the distribution of beer due its domination by the largest brewers; and new market entry at the wholesale and retail level. However, over the years the focus of these investigations has shifted in light of the structural changes that have occurred in both industries. Today the operation of the beer tie is still the primary concern in the distribution of beer, but with pubcos standing in the place of national brewers; and the increasing market presence of the supermarket forecourt and its associated implications has largely displaced concerns over oil company-owned sites. This increased role now played by supermarkets in the distribution of petrol, has been shown to bear some similarities to the increased role they also play in the retail distribution of beer and petrol in the other geographical markets considered in Chapter 5, and most notably Australia. Consequently, by contrast to pubcos which have been accused of inflating beer prices, in

³²⁵ Ibid at para 5, p6

the UK petroleum market the competition authorities have investigated supermarkets' pricing practices, with allegations being made of predation and pricing below the wholesale level, with the ability of independent retailers to compete fairly with them also being called into question. However, as has been shown, in contrast to the Australian position, both sectors, with the exception of the Beer Orders, have been repeatedly cleared of any anticompetitive practices.

Various reasons have been provided in explanation for the repeated failures to identify any anti-competitive practices within either sector. As noted above, in the distribution of beer, in addition to deferring to the EU's acceptance of the tie as a legitimate business model, the OFT has pointed to the fact that consumers benefit from competition and choice between public houses, despite their continuing decline in number; that fragmentation within the market prohibits coordinated behavior; and that retail competition is manifest in increased capital expenditure on amenity and service provision not reduced prices. With regard to the distribution of petrol, when considering the possibility of predatory practices by supermarkets, the OFT has generally been satisfied that so long as competition between oil companies and supermarkets continues, competition will not suffer, even if the number of independent dealers continues to decline; and diversity of suppliers makes collusive behavior difficult at the wholesale and retail level. Further, in accounting for significant variations in pump prices, the OFT has sought to place reliance on cost factors, such as transportation, as well as levels of local competition between wholesalers and retailers. This is despite the fact it has been forced to undertake investigations into practices in local areas, mainly in rural Scotland, in respect of which it has acknowledged the possible existence of competition issues in the wholesale and retail supply of fuel. Further, given the general mistrust surrounding the operation of these markets as a whole, and due to the largely unrelenting campaigning by pressure groups in both sectors, both have been subjected to continued recommendations that they be kept under review.

Nevertheless, whilst continuing declarations of competitiveness in the face of general mistrust over the operation of these markets is just one of the many similarities in the distribution of beer and petrol, there are certain features distinguishing them. These should be taken into consideration when determining whether any guidance can be provided by the distribution of petrol when proposing reforms to the UK beer market. As discussed above, petrol's homogenous nature has meant that issues of restrictions on consumer choice, which have been prevalent in relation to the operation of the beer tie, have not been of such concern in the use of solus agreements. Further, beer has two main, and directly

competing avenues of distribution to the final consumer, as opposed to only one for petrol. Although public houses have traditionally been the principal avenue for the distribution of beer in the UK, increased demand for cheaper off-trade beer has seen supermarkets increasingly dominate this avenue of supply. Consequently, similarly to the distribution of beer in Australia, and also in the US and Belgium discussed in Chapter 5, given the demand for low alcohol prices supermarkets have rapidly gained market share in the UK off-trade by offering beer at greatly reduced retail prices compared with other off-trade outlets which have struggled to compete. The increasing market share enjoyed by supermarkets has significantly altered the structure of the UK off-trade, prompting the decline of the traditional off-license retailers and causing competition within it to be less robust than it has been.

Notwithstanding the differences identified, it is however clear that the distribution of beer and petrol share many similarities, including the increasingly significant participation of supermarkets in the distribution of products within both sectors. This growing participation by supermarkets also appears to be an increasingly global trend. Subsequently, notwithstanding the fact that UK supermarkets have generally reduced prices for consumer and have managed to evade any findings that they are engaging in anticompetitive practices in the retail distribution of petrol, due to the largely unrelenting concerns surrounding their participation in this market, it is suggested that their rapidly continuing growth and its associated implications should be taken into consideration when reforming the regulation of the UK beer market. This is especially so as any proposals to reform the beer tie in the UK on-trade will most likely result in increased beer sales via the directly competing off-trade and so through supermarkets which, similarly to their Australian counterparts, have already attracted the attention of the UK competition authorities in the supply of groceries which includes beer. It is therefore useful in the next chapter to build on this, as well as the critical examination of the provisions of the newly adopted 2015 Act in Chapter 4, and the lessons learned from the consideration of selected geographical markets in Chapter 5, to make proposals for the reform of the regulation of beer distribution in the UK.

Chapter 7 - Conclusions and Recommendations

This Chapter details the conclusions of the thesis. It also draws on the comparative research conducted in the two preceding chapters in order to make recommendations for the future reform of the distribution of beer in the UK. In Chapter 5 a selective comparison of the UK beer market with other non-UK brewing markets was conducted in order to establish how they have dealt with the distribution of beer, and in the preceding chapter the UK beer market was compared with the UK petroleum market, as it shares several of its characteristics including being a scale economy industry with a natural tendency towards vertical integration, causing significant reliance to be placed on tying agreements. However, in order to make such recommendations for reform, in addition to relying on these comparative chapters the historical significance and role of the tie in the UK market, the lessons learned from previous Government interventions, namely the Beer Orders, and their resulting implications for the market, and the Government reforms detailed in the Small Business, Enterprise and Employment Act 2015 (2015 Act) will also be considered and drawn on.

The Chapter first details the conclusions of the thesis (Subsection 1). It then focuses on the peculiarities of the UK beer market that potentially complicate the process of reforming the distribution of beer in the UK (Subsection 2). The Chapter then considers why the tie should not be outlawed in the UK as an illegitimate business model (Subsection 3). It then details recommendations to rebalance the beer tie in the UK (Subsection 4). Finally concluding observations are noted on the recommendations made in this Chapter (Subsection 4).

1. Conclusions

The main objective of the thesis was to examine the competitiveness of the methods by which beer has been distributed in the UK, focusing on the beer tying agreement, with the primary objective of setting out recommendations that better address the on-going anti-competitive concerns associated with the operation of the beer tie today and ensure a socially acceptable level of workable competition. In order to achieve this objective, Chapter 2 addressed the historical development of the UK beer market and sought to establish why the beer tie has been such an integral part of its development up to and including the 21st Century. In the course of this review it became apparent that there are many links binding the brewing industry and the public house market, with the beer tie

being a fundamental part of the UK's brewing business. It also became apparent that reliance on the beer tie has been a source of concern, from as early as 1817, with these anticompetitive concerns persisting through the ages, culminating in the Monopolies and Mergers Commission's (MMC) 1989 Report and the resulting Beer Orders. These were shown not to be the most appropriate response to the complex monopoly then existing amongst the Big Six national brewers at that time.¹ The MMC were deemed to have failed in their aim of increasing competition in the UK market with the Beer Orders also being identified as an important indicator of the unintended consequences that can arise from interfering in the use of the beer tie. The research established that their most significant consequence was the emergence of the pub company (pubco) with these replacing the national brewers in their ownership of significant tied estates of public houses (pubs) thereby preserving the use of the beer tie today.

Chapter 3 of the thesis subsequently addressed the position at the European Union (EU) level given its strong competition law regime geared towards opening up markets to competition, in order to identify how the EU competition law rules have been applied to the brewing industry which relies significantly on beer tying agreements, having the opposite effect. The research demonstrated that initially such agreements were treated in a defensible manner by the European Commission, with this being influenced by the goals of EU competition law, most notably integration. However it was established that a gradual tolerance has been shown towards these resulting in such vertical agreements benefitting from the offer of exemption under the prevailing block exemption Regulation (BER) or by virtue of the application of Article 101(3) Treaty on the Functioning of the European Union (TFEU). Such has been the level of tolerance that the Commission's practices have been shown to demonstrate what Everreste describes as a 'special deference' towards these.² In light of the potentially anticompetitive effects of such vertical restraints, successive BERs have sought to limit their scope and duration, but this has been caveated to the extent that the time limits imposed are inapplicable to beer supply agreements where the goods or services are sold by the buyer from premises and land owned by the supplier or leased by them from third parties. This was shown to be supplemented by the decisional practice of the European Commission and to have been maintained under the provisions of

¹ Chapter 2, p48

² D.A Everreste, 'British and European Community regulation of the British Beer Market: Tapping into the tied house system (Cheers!)' (1990) 20 Ga. J. Int'l & Comp. L. 583 at 610

the current BER 330/2010.³ This review therefore established that the EU regards the beer tie to be a legitimate business model.

The thesis subsequently examined in Chapter 4 how the UK Government has regulated the beer tie, noting any influence exerted by the EU's tolerance of such arrangements. It was demonstrated that while the UK courts initially grappled with the enforcement of the EU competition law provisions, the relationship between the two regimes has developed, including the harmonisation of the legal provisions applicable to beer tying agreements. Nevertheless, the research established that over the course of the decade following the Office of Fair Trading's (OFT) 2000 decision that the UK market was sufficiently competitive for the Beer Orders to be revoked, concerns over the extensive use of beer tying agreements persisted. Over this period it was shown that there was reluctance by the OFT and subsequently the UK Government to intervene in the market, the unforeseen consequences of the Beer Orders being identified as having a chilling effect on such further intervention. The OFT was also shown to frequently defer to the EU's on-going acceptance of the beer tie as a legitimate business model in order to avoid intervening in the market. The first substantive attempt to reform the industry since the Beer Orders was shown to have occurred earlier this year when the 2015 Act received Royal Assent. This introduced a statutory Pubs Code incorporating a Market Rent Only (MRO) option as well as an adjudicator to oversee it. However a critical analysis of these provisions highlighted certain issues with the 2015 Act. It was therefore established that it had to be determined whether the MRO option detailed in the 2015 Act represents the best option for reform of the UK market.

As such, in Chapter 5, comparative research was conducted in order to consider how other geographical markets, namely the United States (US), Australia and Belgium have dealt with beer distribution. This made it possible to determine whether some guidance could be gleaned from these markets on how best to reform the UK beer tie. An examination of the US and Australian markets revealed a broad trend between outlawing the beer tie and considerable consolidation following, while the Belgian beer market, which tolerated the beer tie as a legitimate business model under a legal regime very similar to that in the UK, was shown to be preferable. It is therefore concluded that while the operation of the beer tie in the UK should not be prohibited outright, in the context of the UK market it required to be rebalanced.

³ Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices ((2010) OJ L102/1)

The thesis subsequently examined in Chapter 6 whether another market, namely the petroleum market in the UK, has had the same or similar issues as the distribution of beer in the UK. This comparative research revealed many similarities between the distribution of beer and petrol including numerous and on-going anticompetitive concerns over the operation of both of these sectors over the past several decades. However the research demonstrated that the focus of these investigations had shifted within the petrol industry from concerns over the use of exclusive purchasing agreements to the increasing market presence of supermarkets and their low cost pricing strategies. It was also highlighted in the course of the comparison that supermarkets have an increasing role in the distribution of beer via the off-trade channel, with this development prompting the conclusion that supermarkets' rapidly continuing growth, and its associated implications, should be taken into consideration when making recommendations for the reform of the regulation of the UK beer market.

As noted above, however, in the final year of the research, the 2015 Act became law and makes substantive changes to the operation of the beer tie in the UK. Although the thesis supports the reforms introduced by the 2015 Act as they have gone some way to meet the concerns identified in the thesis, it was submitted in Chapter 4 that these reforms have not gone far enough and there are some risks associated with the provisions of the 2015 Act that could be minimised. The remainder of this Chapter therefore considers the factors that are deemed to be influential, in light of the foregoing conclusions, when making recommendations for the reform of the beer tie in the UK, and, subsequently, details the recommendations proposed by the thesis.⁴

2. The Peculiarities of the UK beer market

As noted above, from the review of the historical development of the UK beer market in Chapter 2 it is apparent that the beer tie has long been an integral feature of the market with significant dependence being placed on the beer tie in order to ensure the efficient distribution of beer in the UK. Consequently, vertical integration between production and retailing has been a feature of the market almost since its inception with the beer tie being interwoven into the market structure, and, subsequently, helping to shape it. This reliance on vertical integration is not however unique to the UK beer market. As noted above, the UK petroleum market is also a scale economy industry and as such producers within that market have also strived to achieve vertical integration in a similar fashion, namely

⁴ For clarity, in the remainder of the Chapter, the reforms introduced by the 2015 Act shall be referred to as the 'Government's Reforms'. The recommendations made in the thesis to strengthen the provisions of the 2015 Act will be referred to as 'Recommendations'.

ownership of retail outlets and the use of exclusive purchasing agreements. Further, from the consideration of the US, Australian and Belgian beer markets in Chapter 5, the use of beer tying agreements and ownership of retail outlets has been of significance in the development and operation of these markets. However, with the exception of the Belgian market, significant measures have subsequently been taken in these other beer markets to either outlaw or limit the use of beer tying agreements due to concerns associated with their use by brewers.

Notwithstanding this, the UK market has more recently come to be distinguished from its counterparts due to the presence of the pubco. Today, due to the Beer Orders and the subsequent emergence of pubcos, the UK market is differentiated from the Belgian beer market, as well as the beer markets in all other EU Member States.⁵ Despite the different approaches to the distribution of beer adopted in the US and Australia, these markets have also not faced any issues with pubcos, as they are not known to exist in these markets. This is due to the fact, as noted above, the emergence of the pubco was an unforeseen consequence of the Government's first significant intervention in the UK beer market, namely the Beer Orders, in an attempt to address the on-going anticompetitive implications associated with the operation of the beer tie at that time. Consequently, the UK market is now distinguishable from its counterparts on account of the presence of pubcos, the emergence of which highlighted the market's resourcefulness and resilience when the operation of the beer tie is threatened. As discussed in Chapter 4, this serves as a reminder of the difficulties that will be faced in making any proposals to reform the distribution of beer in the UK that threaten the operation of the beer tie given the powerful players involved in the market and the complexity of the relationships between them, which have their roots in the historical tied house system.

However despite these difficulties and the potential for further such unintended consequences on intervening in the operation of the beer tie, consideration in Chapter 4 of the ongoing anticompetitive implications associated with its operation in the UK highlight that the beer tie requires to be restricted in order to address these many issues.

3. The tie should not be outlawed as an illegitimate business model

While it is recommended here that the beer tie requires to be restricted in some manner in order to address the many on-going concerns surrounding its operation in the UK market,

⁵ In *Inntrepreneur and Spring*, the European Commission noted the presence of pubcos as one of the factors distinguishing the UK market from that in other Member States. (Commission Decision of 29 June 2000 in Cases IV/36.456/F3 *Inntrepreneur* and IV/36.492/F3 *Spring* ([2000] OJ L195/49) at para 44, 55)

as noted in Chapter 4, successive enquiries have highlighted the abolition of the tie as a simple option for reform, but have refused to recommend this due to the potential implications, with the unforeseen consequences associated with the Beer Orders being highlighted. Further, as noted above, in Chapter 5 in the context of the US and Australian beer markets, it has been concluded that outlawing the beer tie as a legitimate business model is not the most appropriate option for reform and as such is not recommended here. Although consolidation has been a global trend in the international beer market due to, amongst others, technological advances, declining consumption, and the desire for scale economies, it was apparent from reviewing the development of these markets that there is a broad trend between outlawing the beer tie and ensuing rapid consolidation. Today the US and Australian markets are characterised as duopolies.⁶ However, in addition to increasing concentration in these markets outlawing the beer tie also prompted brewers in both jurisdictions to focus on non-price competition such as advertising costs, thereby raising barriers to market entry. Prohibiting the tie subsequently denied smaller brewers the protected market shares they enjoyed from being able to serve their own products in their own retail outlets, causing them to be forced from the market during periods of consolidation as the national brewers came to dominate. By contrast, as discussed in Chapter 2, the UK market through its toleration of the beer tie has long afforded smaller brewers some protection in retaining their market share. This has potentially contributed to the fact that the UK beer market, with the exception of Germany, is now home to the most brewers in the EU.⁷

As noted above, consideration of the Belgian beer market in Chapter 5 further supports this proposition that generally recognising the beer tie as a legitimate business model is not in itself objectionable. While concentrated, today both the Belgian and UK markets are less concentrated than their Australian and US counterparts.⁸ Although other factors have undoubtedly been influential beyond the beer tie, including the largest brewers' desire to maintain a portfolio of brands, Belgium has, under a legal regime not significantly dissimilar to the UK's, managed to retain its trademark diversity which has been lacking in the US and Australia and is only recently returning. As discussed in Chapter 5, smaller brewers have only recently regained some market share in the US with this growth being

⁶ Chapter 5, p166 and p190

⁷ The growth in the number of micro and craft brewers in the UK has been influenced by many factors, not just the toleration of the beer tie. For example, in 2013 the alcohol duty escalator for beer was scrapped, thereby boosting the industry. B Berkhaut et al, 'The contribution made by beer to the European Economy', (Ernst & Young, 2013) <[http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/\\$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf](http://www.ey.com/Publication/vwLUAssets/EY_-_The_Contribution_made_by_Beer_to_the_European_Economy/$FILE/EY-The-Contribution-made-by-Beer-to-the-European-Economy.pdf)> accessed 2nd July 2015

⁸ Chapter 5, p204

assisted by limited exceptions to the 3-tier system and so the prohibition on the beer tie, in order to allow brewpubs to operate.⁹ Similarly, in Australia there has only recently been a resurgence in the craft beer sector. This has not, however, required any amendments to the competition law regime given that vertical integration is permitted in certain circumstances.¹⁰ Nevertheless, these smaller brewers are faced with similar issues to their counterparts operating in the UK market, despite Australia's stricter approach towards exclusive dealing, including foreclosure from many on-trade outlets. Consequently, a general prohibition on exclusive dealing as in Australia does not address the anticompetitive concerns facing the UK market.

It is therefore a primary and general Recommendation of the thesis that the UK, in-keeping with the approach of the EU noted above,¹¹ should continue to recognise the beer tie as a legitimate business model. However, it is suggested in light of the peculiarities of the UK beer market discussed above, namely the existence of the pubco, and the numerous and on-going anticompetitive concerns surrounding their operation of the beer tie, that while the beer tie should not be prohibited outright, in the context of the UK market it requires to be rebalanced.

4. Proposals to 'rebalance' the beer tie in the UK

As noted above and discussed in Chapter 4, despite years of refraining to intervene in the market, the UK Government has recently responded to the on-going concerns regarding the UK beer market that have followed the Office of Fair Trading's (OFT) 2000 decision to revoke the Beer Orders.¹² In doing so, it noted the considerable history of beer tie agreements in the UK. It also highlighted their significance in promoting the growth of small and medium sized brewers, pointing to the buoyant craft beer industry in support of its proposition that the existing industry structure is beneficial to brewers.¹³ The final reforms, namely the statutory code incorporating a MRO option and an adjudicator to enforce it, are now detailed in Part 4 of the 2015 Act.¹⁴

⁹ Chapter 5, p168-170

¹⁰ Chapter 5, 192-195

¹¹ See also Chapter 3.

¹² See Chapter 2

¹³ Chapter 4, p139

¹⁴ Chapter 4, p143

The 2015 Act has ‘two fundamental purposes’ namely to encourage the growth of small companies and to ensure the UK is regarded as a ‘trusted and fair place’ to do business.¹⁵ As mentioned in Chapter 4, the Government at the time of its decision to implement the statutory code and adjudicator therefore clarified that it was not intervening on the basis of competition law considerations, deferring to the OFT’s position that there were no significant competitive concerns over the operation of the UK market.¹⁶ The 2015 Act subsequently reiterates that the Pubs Code implemented by it is to be consistent with the Government’s two main aims of ensuring fair and lawful dealing by pub owning businesses in relation to their tied pub tenants; and the principle that tenants should be no worse off than they would be if they were not subject to a product or service tie.¹⁷ In light of this, it is recommended in the thesis that the Government’s Reforms should be improved upon from the perspective of addressing the numerous and on-going and anti-competitive concerns over the operation of the market. As discussed in Chapter 4, there are several issues associated with the Government’s Reforms. However as they represent an attempt to rebalance, as opposed to outlawing the beer tie as a legitimate business model, the provisions in the Act themselves will form the basis for the proposals in the thesis to reform the distribution of beer in the UK. As such the thesis’ proposals are based on the implementation of the statutory code of practice. In Chapter 4 criticism was levied at a statutory code as a basis for the regulation of the market given the past failings by the industry to adhere to such a code.¹⁸ It is acknowledged that whilst the observation is correct this is, however, the first statutory code to be implemented. Further, in light of the ingenuity expected from the market in responding to the Government’s Reforms and the Recommendations, given its reaction to the Beer Orders in the early 1990s, it is beneficial to have the flexibility that comes with regulation based in secondary legislation in order to deal with any unintended consequences.

4.1 A uniform system of regulation

As discussed in Chapter 4, one of the primary concerns expressed over the Government’s Reforms was their limited application to pub owning businesses with 500 or more *tied* pubs.¹⁹ By including a threshold based on quantity, it has the potential to create a two-tier

¹⁵ HC Deb 16th July 2014, col 906

<[http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm140716/debtext/140716-0002.htm - 14071659000001](http://www.publications.parliament.uk/pa/cm201415/cmhansrd/cm140716/debtext/140716-0002.htm-14071659000001)> accessed 7th June 2015

¹⁶ Chapter 4, p137

¹⁷ Chapter 4, p143-144

¹⁸ Chapter 4, p143

¹⁹ Chapter 4, p145

system of regulation for pubcos falling above and below this threshold.²⁰ Such an approach is reminiscent of the provisions of the Tied Estate Order discussed in Chapter 2, which imposed a threshold of ‘more than 2,000 licensed premises’ as the basis for its application, thereby restricting it to the six largest brewers at that time.²¹ This Order had many unintended consequences, including facilitating the development of the pubco. Therefore, the first Recommendation is that this threshold is removed thus reducing the risk of an unexpected market response.

The danger of a threshold approach lies in the fact there is a large sector of the market which is unaffected by the Government’s Reforms, thereby giving powerful and resourceful market participants the necessary impetus to restructure their affairs in order to come within the unregulated sector. This causes unintended consequences. It also creates loopholes. As discussed in Chapter 4, by focusing solely on the tied pubs of pub owning businesses, the managed pubs and pubcos, as well as those owning fewer than 500 tied pubs, are out with the scope of the Government’s Reforms.²² The Recommendation to include these other categories reduces the risk of brewers and pubcos taking measures to restructure their affairs, such as the sale of some of their pubs or the conversion of a small number of them to the managed model, in order to avoid the application of the Government’s Reforms.²³ By removing the threshold, such measures will be rendered redundant as the 2015 Act will be applicable regardless of how many pubs are operated or the manner in which they are operated.

One of the primary motivations behind the threshold approach of the Government’s Reforms was however the removal of small regional and family brewers from their scope.²⁴ As noted above, the existing regulatory regime has permitted the growth of a large number of brewers, primarily small and microbrewers, with the operation of the beer tie long being considered central to their success. The importance of this model and the need to maintain this growth is fully accepted. However, there is an equal need to ensure that the Government’s Reforms and the Recommendations do not have unintended consequences. It is submitted that uniform application of these to all pubs is the most appropriate solution

²⁰ Chapter 4, p146-147

²¹ Chapter 4, p145

²² Chapter 4, p148

²³ Chapter 4, p146

²⁴ Chapter 4, p146

to reduce this significant risk.²⁵ As already noted, the Government's Reforms and the Recommendations do not seek to outlaw the use of the beer tie which would have a detrimental effect on smaller brewers. The Recommendations are intended to enhance their opportunities under the Government's Reforms to gain market share through increased access to retail outlets for their products and via enhanced distribution arrangements. Such arrangements have long been a source of concern for smaller brewers in the UK and in the other geographical markets selected for comparative analysis in Chapter 5. Further, as noted in Chapter 4, the operation of the beer tie by smaller and family owned brewers has not been entirely without concern which further supports the Recommendation for a uniform system of application applicable to all market participants.²⁶

4.2 Preservation of stocking obligations

As noted above, retaining and promoting the success of the UK's variety of brewers is an important consideration in making Recommendations. Section 68(5) of the 2015 Act subsequently removes stocking obligations in respect of beer and cider from the scope of Part 4 of the Act.²⁷ This approach is welcomed and would have been a Recommendation of the thesis had this not been met by the Government's Reforms, due to their deemed importance discussed in Chapter 4, in protecting the market position of brewing pubcos and small and regional brewers.²⁸ Such obligations have the advantage of affording brewers the protection of requiring that their products be sold from their own premises but allows the tenant the protection of sourcing these on the open market from any supplier they wish, thereby reducing the possibility that they are forced to pay anticompetitive prices for those brands. The brewer has to compete for the tenant's business and so offer the best price for their products.²⁹ The stocking obligation also precludes the tenant from being prohibited from selling on the premises competing suppliers' beer or cider, thereby introducing increased consumer choice and flexibility for the tenant to respond to changing consumer preferences. However, as noted in Chapter 4, it will be essential that the brewer does not circumvent this by ensuring that they are the only source from which their brands

²⁵ The only exception to this is free houses. These are free-of-tie pubs which choose to be supplied by a particular pubco, brewer or wholesaler. This is deemed not to increase the unintended consequences of the Recommendations. These pubs operate at arm's length from the pubco or brewer and have the freedom to source the beers they serve on the open market and so not at inflated prices, from their supplier of choice.

²⁶ Chapter 4, p145-146

²⁷ Chapter 4, p150

²⁸ Chapter 4, p150

²⁹ Chapter 4, p150

can be bought.³⁰ Such potential implications are however unavoidable and as such require to be managed effectively by the adjudicator.

4.3 The Market Rent Only (MRO) option

Section 43 of the 2015 Act details the most controversial of the Government's Reforms to the beer tie, namely the MRO option. The MRO option essentially frees the tenant or licensee of any ties to their landlord and obligates them to pay only the market rent for the property.³¹ The second Recommendation is to make the MRO option available to all prospective or existing pub tenants and licensees in order to rebalance the beer tie in the UK. This is however a significant market intervention which greatly weakens the operation of the beer tie. Therefore, in recognition of the importance of preserving the operation of this business model in the UK market, the Recommendation is that the MRO option whilst available to all tenants and licensees must only be available under very limited and clearly defined circumstances, which will be set out below.

The MRO option however potentially addresses many of the on-going anticompetitive concerns over the operation of the beer tie discussed in Chapter 4 and essentially allows the market to decide whether or not the tied or free-of-tie model is best rather than imposing a mandatory free-of-tie business model on the market.³² While concerns have been expressed that the MRO option will cause investment in pubs to cease, should a tenant or licensee be in a relationship with a Landlord under which they benefit from such investment or other benefits, it is submitted that it is highly unlikely that they would accept the MRO offer, and so change their contractual arrangements with the landlord, thereby reducing the potential for this to occur. As noted in Chapter 4, the MRO option also offers the potential benefit of opening up retail outlets to competing brewers' products thereby reducing barriers to entry for small and new brewers seeking a distribution channel for their products. This subsequently reduces the risk of market foreclosure, as well as increasing consumer choice should MRO tenants and licensees choose to stock a wide range of brands.³³ MRO tenants and licensees can also source these brands on the open market, rather than from their landlord at inflated wholesale prices, which should result in lower retail prices for consumers.³⁴

As stated above, this second Recommendation is subject to conditions.

³⁰ Chapter 4, p150

³¹ Chapter 4, p152

³² Chapter 4, p139

³³ Chapter 4, p139-140

³⁴ Chapter 4, p120

4.3.1 Circumstances under which MRO option is to be offered

Section 43 of the Government's Reforms details numerous circumstances under which the MRO option is to be offered. As noted in Chapter 4, many of these circumstances are subjective and so lacking in certainty thereby potentially extending the application of these provisions, and causing uncertainty, which greatly undermines the operation of the beer tie.³⁵ By contrast, the second Recommendation is that this option be available only on two clearly defined occasions.

Firstly, at the time the tenancy or licence agreement is entered into between the parties. The Government opted not to make the MRO option available to prospective tenants, instead placing reliance on the flawed parallel rent assessment under the provisions of the 2015 Act.³⁶ However, offering the MRO option at the outset increases transparency by allowing the prospective tenant access to the necessary information to make an informed decision as to which business model to pursue, thereby reducing the possibility of them entering into a disadvantageous contract.³⁷ This ultimately increases the prospect of an effective and efficient business relationship between the parties which is in the interests of the market and ultimately the consumer.

The second occasion on which it is proposed that the MRO option should be offered is 'on the later of the rent assessment or assessment of money payable by the tenant in lieu of rent, or after a period of four years from the commencement date of the tenancy or licence under which the pub is occupied'. This Recommendation is intended to remove the subjectivity and so the uncertainty associated with the Government's Reforms, thereby reducing the potential scope of the MRO option and its weakening effect on the operation of the beer tie. It ensures that existing tenants or licensees are provided with a clear opportunity to decide whether or not to persist with their contractual arrangements with their landlord. Postponing the offer until after a period of at least four years also balances the level of intervention the MRO option represents for the market, with the tenant or licensee's freedom to determine whether they wish to pursue the MRO option.

While this Recommendation potentially denies existing tenants and licensees an immediate solution by delaying the offer of the MRO option by a period of at least four years, the third Recommendation is to phase the implementation of the MRO option and so reduce the impact of this intervention in the market. As discussed in Chapter 2, the Beer Orders

³⁵ Chapter 4, p153-154

³⁶ Chapter 4, p151

³⁷ Chapter 4, p151

sent shock waves through the industry by requiring that their terms be met with by a set compliance date and may have contributed to the unforeseen consequences they had.³⁸ It is therefore necessary to avoid repeating this with the Government's Reforms and the Recommendations. As already mentioned one of the greatest challenges to the Government's Reforms and the Recommendations will be the resourcefulness of the market in attempting to evade their application. By limiting the offer of the MRO option to two clearly defined occasions and phasing its implementation under the third Recommendation should reduce one such risk, namely pubcos converting their tied estates to managed estates in order to avoid being subject to the Government's Reforms.³⁹ This risk is already minimised by the fact that, as discussed in Chapter 2, pubcos are essentially property owning companies. As such they are unlikely to restructure their entire estates, thereby foregoing the rental income generated, in order to evade the MRO option which need only be offered under the limited circumstances outlined by the second Recommendation. It is also even more unlikely where the pubco is also a brewer given their dependence on their tied estates.⁴⁰ Nevertheless this is a risk that should be acknowledged and addressed.

Limiting and phasing the MRO option under the Recommendations should also reduce other concerns associated with its implementation. This includes the potential for pubco estates to suddenly become entirely free-of-tie, which would deny them the benefit of economies of scale. Such a change would limit the pubco's ability to negotiate discounts from brewers as is central to their business model, and was a concern discussed in Chapter 4.⁴¹ The possibility that pubco tenants may opt to pursue the MRO option may however have the beneficial effect of encouraging pubcos to pass on some of these discounts to their tenants, through lower wholesale beer prices, in order to reduce the likelihood of their tenants accepting the MRO option.⁴² Further, phasing the offer of the MRO option under the Recommendations should also reduce the risk that the market will be flooded with free-of-tie pubs in a manner reminiscent of the market effects of the Beer Orders.⁴³

The Recommendations address another concern associated with the MRO offer discussed in Chapter 4, namely the potential for international brewers to dominate the market by offering discounts to MRO tenants in return for exclusivity, thereby causing market

³⁸ Chapter 2, p36

³⁹ Chapter 4, p148

⁴⁰ Department for Business, Innovation and Skills, *Pub Companies and Tenants Government Response to the Consultation* (June 2014) at p72

⁴¹ Chapter 4, p140

⁴² The issue of pubcos passing on discounts was discussed in Chapter 4 at p124

⁴³ Chapter 2, p37

foreclosure.⁴⁴ While the Recommendations will cause there to be a greater number of MRO pubs than under the existing regulatory regime, by limiting and phasing its offer, only a proportion of pubs in the UK should be MRO pubs under the Recommendations. Further some of these will be subject to stocking obligations and so complete exclusivity could not be offered to the international brewers. Consequently these brewers should not be able to achieve the scale necessary to dominate the UK market simply on the basis of the Recommendations, as they were under the Beer Orders.⁴⁵ Further, should tenants and lessees who are free of stocking obligations choose to be supplied by these international brewers, the decision to do so will be influenced by, amongst others, consumer demand for their products. As the majority of pubco estates in the UK are already supplied by these international brewers as they offer pubcos the greatest discounts,⁴⁶ the MRO option should therefore introduce the chance for tenants and licensees to decide whether there is sufficient demand to replace these with other brewers' products, thereby having the opposite effect.

The MRO option subject to the Recommendations subsequently presents the opportunity to increase the level of competition in the UK market without being as extreme and as interventionist as the Beer Orders, thereby reducing the likelihood of unforeseen consequences. Nevertheless, as discussed in Chapter 4, the lack of an independent wholesale and distribution sector in the UK market has been a source of concern since the MMC's 1989 Report.

4.4 Impact on the wholesale and distribution sector

As discussed in Chapter 6, despite sharing many of the characteristics of the petrol industry, the UK competition authorities have tended to be less scathing with regard to the UK petroleum market, by comparison to the UK beer market, on account of its relatively competitive wholesale sector. By contrast, the UK beer market has long lacked such an independent wholesale and distribution sector. Following the Beer Orders, wholesaling and distribution is still dominated by the largest brewers with pubco operating practices being considered to encourage this.⁴⁷ However, as the Recommendations remove the '500 tied pubs' threshold requirement for the offer of the MRO option and extends it to all tenants and licensees, albeit under narrow clearly defined circumstances, and on a phased basis, there will inevitably be a greater number of free-of-tie pubs in the longer term requiring to

⁴⁴ Chapter 4, p140

⁴⁵ Chapter 2, p39

⁴⁶ Chapter 2, p40-41

⁴⁷ Chapter 4, p119

be supplied with beer than under the existing regulatory regime. As noted above, depending on, amongst others, consumer demand, these pubs may opt to serve the products of local and regional brewers. Consequently, the MRO option could increase the likelihood of an independent wholesale and distribution sector emerging to distribute these beers to MRO outlets thereby reducing the international brewers “*stranglehold on the distribution of beer*”.⁴⁸ This could potentially avoid the need for more interventionist measures to achieve this goal, such as mandating divestiture within the distribution sector in order to ease the largest brewers’ grip on the UK market. The MRO option subject to the Recommendations therefore has the potential to facilitate small brewers’ access to distribution arrangements for their products which is an on-going issue facing such brewers not only in the UK but in the other geographical markets discussed in Chapter 5.

4.5 Meeting the challenge presented by supermarkets

Supermarkets however, also have a prominent role in the distribution of beer in the UK off trade market and this could potentially increase under the Government’s Reforms and the Recommendations.⁴⁹ As discussed in Chapter 5, the role of supermarkets in the distribution of beer in the US and Australian beer markets increased following intervention in the operation of the beer tie in the on-trade.⁵⁰ This is due to the fact beer has two directly competing avenues of distribution to the final consumer through the on and off-trade markets.⁵¹ Any proposals to reform the beer tie in the UK on-trade will therefore most likely result in increased beer sales via the off-trade and so through supermarkets. As noted above and discussed in Chapter 6, supermarkets now also have a prominent role in the distribution of petrol in the UK, with their participation in the market being the focus of recent competition enquiries, not suppliers’ reliance on exclusive purchasing agreements. However, in contrast to pubcos which have been accused of inflating beer prices, the UK competition authorities have investigated supermarkets’ pricing practices under allegations that they are engaging in predation and pricing below competitive levels, in the petroleum market. Similar concerns have also been raised in the UK grocery market, although this has not been accepted by the competition authorities.⁵² As discussed in Chapter 5, their practices have also attracted the attention of the Australian competition authorities.⁵³

⁴⁸ Chapter 4, p119

⁴⁹ Chapter 5, p168

⁵⁰ Chapter 5

⁵¹ Chapter 6, p259

⁵² Chapter 6, p262-264

⁵³ Chapter 5, p197. However, as discussed in Chapter 6, increased off-trade sales of beer via supermarkets is a global trend.

Nevertheless, increasing beer prices in the on-trade due to pubcos' failure to pass on wholesale discounts to lessees have subsequently caused pub closures as consumers have turned to lower off-trade sales, primarily those of supermarkets given their low cost pricing strategies.⁵⁴ However the Recommendation for the uniform application of the MRO option and its offer to all tenants and lessees, in conjunction with the acceptance of stocking requirements, increases the likelihood of suppliers' having to price their beer more competitively, which should subsequently filter through to lower retail prices in the on-trade. These Recommendations should therefore potentially reduce retail prices and so also reduce the challenge and competitive implications for the UK beer market resulting from supermarkets' increasing participation.

4.6 Concluding observations

The beer tie has long been an integral feature of the market with significant dependence being placed on this in order to ensure the efficient distribution of beer in the UK. While it is not proposed in the thesis that the beer tie be outlawed as an illegitimate business model, it is recommended that it be rebalanced by building on the Government's Reforms. Given the unforeseen consequences of past market interventions, namely the Beer Orders, the Recommendations seek to mitigate the risk of these arising. It is proposed that this be achieved by removing the threshold of '500 tied pubs' for the application of the Government's Reforms thereby implementing a uniform system of regulation, that the offer of the MRO option be restricted to two clearly defined events in order to remove any subjectivity and to limit the uncertainty associated with its offer, and that the implementation of the proposals be phased in order to avoid sending shock waves through the industry, as the Beer Orders did in the 1990s and thereby potentially contributed to their dramatic impact on the market. However, while it is hoped that these Recommendations will safeguard against such unintended consequences, given the powerful players involved in the market and the complexity of the relationships between them, which have their roots in the historical tied house system, making recommendations is a complicated matter and no perfect solution exists.

As stated at the outset,⁵⁵ the intention of the thesis is not to make recommendations to achieve a state of perfect competition. Rather, it undertakes to make informed recommendations that address better the competition issues in the market today. It remains to be seen whether the MRO option as refined by the Recommendations presents the

⁵⁴ Chapter 6, p259

⁵⁵ See Chapter 1, p3

optimal solution for reform of the beer tie, however it is hoped that given the safeguards outlined above, it should strike the right balance between addressing the on-going anti-competitive concerns associated with the operation of the beer tie and the need to preserve it as a legitimate business model in the UK beer market thereby ensuring a socially acceptable level of workable competition.

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