

Supporting Net Zero: UK CMA Consults on Draft Sustainability Guidance

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03 / 10 / 23

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On February 28, 2023, the UK Competition and Markets Authority (CMA) issued for consultation its long-awaited draft guidance on environmental sustainability agreements (Draft Guidance). The CMA first foreshadowed the publication of this detailed guidance in its March 2022 advice to government.

Key Points

- The Draft Guidance is designed to help businesses seeking to work together on environmental sustainability initiatives by providing greater clarity on how to assess these projects under UK competition law.
- The CMA proposes a broader interpretation of the exemption criteria for climate change agreements, which takes into account the totality of the benefits accruing to all UK consumers rather than limiting eligible benefits to those accruing to consumers in the market affected by the agreement.
- While the CMA is prepared to offer informal advice and comfort on some proposed sustainability initiatives, it will be alert to any proposals that use environmental concerns as a cover for anticompetitive conduct.
- Companies pursuing cross-border collaboration in this area will need to be mindful of the potential for competition authorities to take divergent approaches.

The Interplay Between UK Competition Law and Sustainability

Businesses face increasing pressure to make their operations more sustainable. The fear of a “first-mover disadvantage” is deterring unilateral action which means that, in the absence of effective international regulation, a collaborative approach is necessary to drive and achieve real change.

However, business collaborations with climate-friendly objectives can restrict competition in the same way as any other agreement. UK competition law, which mirrors the EU framework, prohibits anticompetitive agreements (known as the Chapter I prohibition). The consequences of breaching the Chapter I prohibition are serious and can include financial penalties of up to 10 per cent of worldwide group turnover. A general exemption from the Chapter I prohibition exists under specified conditions, and requires businesses to self-assess to consider whether they meet the statutory criteria.

Competition authorities have in recent years been considering whether, and if so how, competition law regimes should adapt to enable more private sector collaboration on sustainability. The debate within Europe has focused on whether the general exemption criteria, which have traditionally been subject to a narrow interpretation, should be construed more expansively to include the wider benefits that could be gained from cooperation on sustainability initiatives. The Draft Guidance sets out the CMA’s proposed policy position on this issue.

Main Points of the Draft Guidance

Focus on environmental initiatives. The Draft Guidance applies to collaboration aimed at achieving environmental sustainability benefits, such as improving air or water quality, conserving biodiversity or promoting the sustainable use of raw materials. The Draft Guidance has a narrower scope than the European Commission’s (EC’s) March 2022 draft sustainability guidance and the January 2021 draft guidance from the Dutch Authority for Consumers and Markets (ACM), which both extend beyond environmental initiatives to wider social objectives such as working conditions and human rights.

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Agreements That May (or May Not) Restrict Competition

Restriction by object or effect. Environmental sustainability agreements can have the “object” of restricting competition in the same way as any other agreement between competitors, in particular those which involve price-fixing, market or customer allocation, limitations of output or limitations of quality or innovation.

The CMA, like the EC in its draft guidance, helpfully clarifies that an agreement between competitors to purchase only from suppliers with a limited environmental footprint should not be characterized as a collective boycott – which is usually an object restriction – as the intention is not to eliminate a competitor. The CMA also sets out factors that are likely to be relevant in considering the “effect” on competition of environmental sustainability agreements, such as the market coverage of the agreement and the ability of non-parties to participate. The CMA notes that agreements which restrict competition by object or by effect are capable of meeting the criteria for individual exemption.

No restriction of competition. A significant number of cooperation initiatives are likely to fall outside of the Chapter I prohibition. While no safe harbour is proposed, the CMA provides extensive examples of the types of environmental sustainability agreements that are unlikely to give rise to competition concerns under seven broad categories:

- i. Agreements which do not affect the main parameters of competition.
- ii. Agreements to do something jointly which none of the parties could do individually.
- iii. Cooperation required by law.
- iv. Pooling information about suppliers of customers.
- v. Creation of industry standards.
- vi. Phasing out/withdrawal of non-sustainable products or processes.
- vii. Industry-wide efforts to tackle climate change.

Individual Exemption for Agreements That May Restrict Competition

The Draft Guidance reviews the four cumulative statutory criteria for exemption in the context of environmental sustainability agreements and provides a more permissive approach in respect of climate change agreements.

Benefits arising from the agreement. The Draft Guidance recognises that benefits can include environmental benefits (e.g., reducing greenhouse gas emissions) as well as other benefits such as developing innovative energy-efficient processes, provided that the benefits are substantiated.

Consumers receive a fair share of the benefits.

- The Draft Guidance largely follows the approach proposed by the EC that it will only be appropriate to take account of any benefits enjoyed by direct and indirect **users of the product covered by the agreement**. Where two markets are related, benefits achieved on separate markets can also be taken into account where consumers affected by the restriction and receiving the benefit are substantially the same or substantially overlap (with no guidance on when this threshold might be met in practice).
- In an important step-change, the CMA accepts that the special sub-category of **climate change agreements** (agreements which contribute towards the UK’s binding climate change targets) should benefit from a broader interpretation of the test which considers the totality of the benefits to all UK consumers. This positions the CMA towards the more liberal end of the current spectrum of approaches, along with the Dutch ACM and Austria which both consider environmental benefits to society at large.
- The CMA is open to interpreting **consumer benefits** more broadly by recognising that consumers may benefit not only directly (e.g., improved product quality or variety) but also indirectly (where consumers value the impact of their sustainable consumption on others). The Draft Guidance explains that parties may use consumer surveys to demonstrate indirect benefits but does not provide parameters on how such surveys should be designed. The Draft Guidance also refers to the possibility of claiming wider environmental benefits (e.g., societal benefits from restricting plastic use).
- The CMA confirms that **future benefits** as well as current benefits are relevant to the assessment, which is important as sustainability benefits are likely to be achieved over a relatively long period of time. The Draft Guidance simply confirms that parties should describe the relevant timeframe as concretely as possible. (Guidelines issued in September 2022 by Austria’s federal competition authority (BWB) state that the time horizon should usually be certain or at least foreseeable.)
- The benefits arising from the agreement **must offset the harm** to competition in each case. The onus is on the parties to demonstrate and, where appropriate, quantify in line with industry best practice, the relevance and weight of the negative effects and benefits of an initiative.
- The CMA recognizes that it may not always be possible for businesses to precisely **quantify environmental benefits**, and points to examples of established techniques that may be used.

Indispensability. It is essential that the restrictions in the agreement go no further than is indispensable to the relevant benefits, and careful consideration should be given to the scope and duration of these restrictions. The CMA provides examples

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of when this condition might be met (*e.g.*, to overcome the first-mover disadvantage) and cautions that it would not be satisfied in cases where there are “enough consumers willing to pay for the sustainable product”, as businesses should compete to satisfy that demand.

No elimination of competition. The Draft Guidance confirms that there must be some remaining competition on the market(s) covered by the agreement.

CMA's Open Door and Enforcement Policy

Comfort is provided by the CMA's statement that it will not take enforcement action against agreements that clearly correspond to the (numerous) examples, and are consistent with the principles, set out in the Draft Guidance.

The CMA is willing to provide informal advice at an early stage regarding the application of the Guidance to specific proposals. The CMA intends to publish non-confidential summaries of its individual assessments. Also, it will not issue fines against parties that implement environmental sustainability agreements which were discussed informally with the CMA in advance, provided that the parties address any competition concerns raised by the CMA and do not withhold information which would have made a material difference to the outcome of its assessment.

Practical Points for Businesses

Meeting sustainability objectives will often require different parties in an industry to reach a consensus on the design and implementation of novel initiatives. Participating businesses will each need to self-assess the compatibility of the project with competition laws and each may have a different legal risk tolerance.

The Draft Guidance provides businesses with much-needed clarity on these complex legal and economic assessments. That, coupled with the CMA's willingness to provide comfort, may help legitimate sustainability projects to get off the ground. The Draft Guidance is not binding on courts, however, so would not prevent private competition litigation being brought.

The more permissive approach for climate change agreements in particular may make it easier for parties to show that their agreement meets the criteria for exemption. An overall positive impact is more likely where wider benefits are taken into account. However, only those wider benefits which extend to UK consumers can be included rather than to society at large. In many cases, it will be clear that the environmental benefits are sufficient to offset the harm such that it will not be necessary for parties to carry out a detailed quantification exercise.

The proposal to proactively publish non-confidential examples of initiatives has the potential to provide further clarity, but will ultimately depend on the willingness of businesses to approach the CMA with bold initiatives involving complex economic analyses.

Crucially, the Draft Guidance may not offer sufficient reassurance to companies pursuing cross-border collaboration, as there is no consensus between different authorities on how to assess sustainability cooperation. The EC guidance is expected to bring a more consistent approach at the EU level when a final version is published in spring 2023, but the guidance as currently drafted does not align with CMA's proposal in many respects. Outside Europe, some competition authorities are willing to use existing public interest exemptions to authorise some sustainability initiatives (*e.g.*, Australia) or are consulting on their own sustainability guidance (*e.g.*, Japan). However, the U.S., in particular, is taking a more conservative approach. Businesses will therefore need to carefully consider the evolving patchwork of legislative initiatives, guidelines and decisional practice when planning industry-led initiatives.

Next Steps

The public consultation on the Draft Guidance runs until 11 April 2023, following which the CMA will include the final version as part of its broader guidance on the application of the Chapter I prohibition to horizontal agreements (which was issued for separate public consultation on January 25, 2023). The CMA may incorporate the practical experience it gains into future versions of its guidance.