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EUROPEAN COMMISSION CLARIFIES SUSTAINABILITY RULES IN REVISED HORIZONTAL GUIDELINES

European Commission clarifies sustainability rules in revised horizontal guidelines

On 1 June 2023, the European Commission published its long-awaited revised guidelines on horizontal cooperation (Guidelines) along with revised Horizontal Block Exemption Regulations on R&D and Specialisation agreements. The Guidelines include a specific chapter on sustainability agreements which aims to better equip businesses to assess compatibility of their cooperation agreements with EU competition rules, where such agreements genuinely pursue sustainability initiatives. This chapter remains largely unchanged from the draft revised guidelines published on 1 March 2022.

The Guidelines and the green transition

The inclusion of the sustainability chapter aligns with policy incentives under the European Green Deal, which aims to set the EU on the path to a green transition whereby all relevant policy areas contribute towards the ultimate goal of climate neutrality by 2050. It is another example of a competition authority seeking to facilitate collaborative efforts to meet sustainable goals within (clearly defined) boundaries of competition law. In the UK for example, we have seen similar intentions from the Competition and Markets Authority (CMA) with the publication of its draft guidance on the application of UK competition law to sustainability agreements in February of this year.[1]

What are sustainability agreements?

The Guidelines include a broad definition of "*sustainability*", which encompasses activities that support economic, environmental and social development (including labour and human rights development).

Similarly, "*sustainability agreements*" are defined as "*any horizontal cooperation agreement that pursues a sustainability objective, irrespective of the form of the cooperation*".[2]

[1] See our prior analysis of this guidance here.

[2] Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (2022/C 164/01), para. 551.

Which sustainability agreements are likely to fall outside the scope of Article 101(1)?

The Guidelines explain that not all sustainability agreements between competitors will be caught by the prohibition on anti-competitive agreements and practices contained in Article 101(1) of the Treaty on the Functioning of the European Union (Art. 101(1)), such as those which do not affect the parameters of competition (including price, quality, choice, innovation, etc.).

Four broad categories of sustainability agreements are identified as unlikely to fall within the remit of Art. 101(1):[3]

- agreements imposing restrictions solely aimed at ensuring compliance with legally binding international treaties, agreements, or conventions. Examples include compliance with prohibitions on the use of certain pollutants;
- agreements that do not concern the economic activity of competitors but only their internal conduct. For example, rival firms may wish to increase their industry's environmental profile, and for this purpose may agree on measures to eliminate single-use plastics from their business premises;
- agreements on the creation of databases containing information on suppliers that have (un)sustainable value chains, use (un)sustainable production processes, or information about distributors that market products in a(n) (un)sustainable manner, but without requiring the parties to purchase from those suppliers or to sell to those distributors; and
- agreements relating to the organisation of industry-wide campaigns on sustainability, providing they do not amount to joint advertising of specific products.

[3] Ibid., paras. 528-531.

Assessment of sustainability agreements that do fall within Article 101(1)

Restriction of competition by object/effect

Typically, where it is clear that an agreement has as its object the restriction of competition (for instance, price fixing or market sharing), it is not necessary for the enforcing authority to prove that the agreement will produce anti-competitive effects as the 'object' itself demonstrates a sufficient harm to competition. The Guidelines provide some examples of sustainability agreements deemed to be anti-competitive by object - specifically in the context of sustainability standardisation agreements (i.e., agreements between competitors relating to the adoption of an industry standard on sustainability). These are:[4]

- agreements between competitors to pass increased costs resulting from the adoption of a sustainability standard onto customers; and

- an agreement between competitors to limit technological development to the minimum sustainability standards required by law, instead of cooperating to achieve more ambitious environmental goals.

However, the Guidelines provide that where the parties to an agreement substantiate that the main object of an agreement is the pursuit of a sustainability objective, and where this casts reasonable doubt on whether the agreement reveals by its very nature, a sufficient degree of harm to competition to be considered a by object restriction, the enforcing authority will have to assess the agreement's effects on competition.

The Guidelines contain a "*soft safe harbour*" in the effects analysis for sustainability standardisation agreements (there is no equivalent for other types of sustainability agreements). When the following six cumulative conditions are met, the agreement will not be considered to have adverse effects on competition within the scope of Art. 101(1):[5]

1. Standard development must be transparent and participative.

2. The standard should be adopted on a voluntary basis and access should be open to all market participants.

3. Undertakings should be able to adopt stricter standards.

4. The parties should not exchange sensitive commercial information.

5. Access to the outcome should be effective and non-discriminatory.

6. Sustainability standards must satisfy at least one of the following two conditions:

    a. should not lead to a significant increase in price or a significant reduction in the quality of the products on the market; and/or

    b. The combined market share of the undertakings must not exceed 20% on any relevant market affected by the standard.

Failure to comply with one or more of the conditions does not automatically create a presumption that the agreement restricts competition within the meaning of Art. 101(1), but the negative appreciable effects of the agreement will then need to be assessed in the normal way (taking into account factors such as the market power of the parties, market coverage of the agreement, extent of (if) any commercially sensitive information exchange, etc.).

However, there remains a lack of clarity as to the first limb of the sixth cumulative condition. The Guidelines contain no detail as to how any such "*significant*" price increase resulting from a sustainability standard might be appropriately assessed (other than the assessment being dependent upon the characteristics of the product and of the relevant market). Given the issue of "*first-mover disadvantage*" (often resulting from higher costs associated with sustainability standards), it remains unclear why the Commission did not include more concrete guidance in this respect.

Analysis of sustainable benefits under Article 101(3)

In general, when assessing whether an agreement producing appreciable negative effects on competition may benefit from the exemption provided by Art. 101(3), the parties have to prove that the agreement meets the following four cumulative conditions: (i) that the agreement contributes to "*objective, concrete and verifiable*" **efficiency gains**; (ii) that the restriction of competition is **indispensable** to the attainment of benefits; (iii) that **consumers receive a fair share of the purported benefits**, when the benefits outweigh a restriction of competition; and (iv) parties continue to compete on at least one parameter of competition (i.e., **the agreement does not eliminate competition** from the relevant market).

Condition (iii) - the requirement that consumers receive a fair share of the purported benefits - has proved tricky in the context of sustainability agreements where benefits may accrue to society as a whole rather than specifically to consumers of the relevant product or service. So how has the Commission tackled this issue in the Guidelines?

"Fair share" of benefits?

The Guidelines contain detailed guidance on whether sustainability benefits can be considered efficiency gains

[4] Ibid., para. 548.

[5] Ibid., paras. 599-600.

for "consumers" – which the Guidelines define as comprising "all direct and indirect users of the product covered by the agreement".[6]

The Guidelines explain that such assessment includes:

- the benefits resulting from direct use of the products covered by the sustainability agreement ("*individual use benefits*" – such as consumers benefitting from better tasting vegetables which were grown organically); and

- those indirect benefits arising from the use of product under a sustainability agreement ("*individual non-use benefits*" – such as appreciation for a cleaning product which uses less chemicals as the indirect benefit to the consumer (as it is less harmful to the environment) rather than a direct benefit where the product results in a superior clean).

In doing so, the Guidelines maintain an approach that ignores the benefits sustainability agreements may bring to wider groups than simply the end-consumer(s). This approach differs to that of (1) the CMA, which, in its draft sustainability guidance, permits the exemption to apply to agreements if the 'fair share' condition can be satisfied when taking into account the totality of the benefits accruing to all UK consumers, as opposed to apportioning those benefits between consumers within the market affected by the agreement and those in other markets (albeit only in respect of 'climate change agreements') and (2) the Dutch Authority for Consumers and Markets (ACM), which, in its **draft guidelines on sustainability agreements**, goes even further, by stating that when assessing 'environmental-damage agreements' consumers may not need to be fully compensated where such agreements comply with an international or national standard or help realise a concrete policy goal.

Although the Guidelines do provide a mechanism for "*out of market*" benefits to be considered, as "*collective benefits*", this is only permitted in those circumstances where consumers in the relevant market substantially overlap with (or are part of) the beneficiaries outside the relevant market. For example, consumers may purchase clothing made from cotton produced overseas using less chemicals and less water, resulting in less runoff of pesticides on the land where the cotton is cultivated. As the environmental benefits arising from such sustainable cotton will occur or be likely to occur in the local area where the cotton is grown, these environmental benefits are unlikely to accrue to the consumers in the relevant market due to a lack of 'substantial overlap'. By retaining the approach which requires full compensation to consumers in order to rely on the Art. 101(3) exemption, an opportunity is missed for greater global alignment in sustainable efforts.

Concluding Remarks

Overall, the Guidelines are a positive development for EU competition law as they provide helpful clarifications for businesses on the interplay between collaboration on sustainability initiatives and the limits of EU competition law. Although as noted the Commission may not have been as ambitious as it could have been in relation to the fair share criterion for application of the Art.101(3) exemption.

It will be interesting to assess what impact the Guidelines will have in encouraging businesses to invest in new sustainability initiatives, as well as the response of other European competition authorities such as the ACM.

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