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A path to greener collaborations – CMA publishes guidance on sustainability agreements

On 28 February 2023, the Competition & Markets Authority ("**CMA**") published its long-awaited draft guidance on environmental sustainability agreements ("**Draft Guidance**").[1] The CMA, like many regulators, is seeking to provide more clarity and certainty on the potential antitrust risks competing businesses may face should they collaborate to meet environmental, social and corporate governance ("**ESG**") objectives. Therein lies a tricky balance. On the one hand, the private sector undoubtedly has a key role to play in facilitating a shift to a "greener" economy, but any competitor collaborations on ESG initiatives can bring an increased risk of anti-competitive collusion (including price fixing, market or customer allocation, limitations of output, quality or innovation, or collective boycotts).

The Draft Guidance provides an initial insight into the CMA's position on this issue, and with it a welcome indication that the CMA plans to take a constructive, more flexible and permissive stance than some other regulators worldwide.

What does the Draft Guidance cover?

The main purpose of the Draft Guidance is to assist businesses in self-assessing when their ESG collaborations are likely or unlikely to be caught by the prohibition on anti-competitive agreements contained in Chapter I of the Competition Act 1998 ("**Chapter I prohibition**").

The Draft Guidance identifies two main types of collaboration arrangements that would qualify as pursuing a generally "green" objective and which would fall within its scope:

- **Environmental Sustainability Agreements ("ESAs")**: The CMA has kept the definition of these agreements relatively broad and they include agreements or concerted practices between actual or potential competitors which are aimed at preventing, reducing or mitigating the adverse effect their economic activities may have on environmental sustainability. The Draft Guidance gives some examples, including agreements aimed at improving water and air quality, conserving biodiversity or promoting the sustainable use of raw materials. Importantly, any broader social objectives which do not directly relate to environmental sustainability, such as working conditions and animal welfare standards, are outside the scope.[2]
- **Climate Change Agreements ("CCAs")**: These are a subset of ESAs and cover agreements which contribute towards the UK's binding climate change targets (e.g., Net Zero). Examples of these types of agreements include arrangements to phase out certain product processes which involve the emission of carbon dioxide or arrangements not to provide financing or insurance support to fossil fuel producers.

Self-assessment process

The Draft Guidance discusses three categories of ESAs: (1) those that are unlikely to infringe the Chapter I prohibition; (2) those that could infringe the Chapter I prohibition; and (3) those that could benefit from an individual exemption under the criteria contained in Section 9(1) of the Competition Act 1998 (i.e., where the agreement in question meets a set of specified criteria, including the requirement that the procompetitive benefits of such an agreement outweigh any otherwise anti-competitive elements).

1. Agreements which are unlikely to infringe the Chapter I prohibition

These include ESAs that:

a) do not relate to the way businesses compete with each other (e.g., on price, quantity, quality, choice or innovation) or because they

[1] The Competition & Markets Authority. *Draft guidance on the application of the Chapter I prohibition in the Competition Act 1998 to environmental sustainability agreements*. 28 February 2023. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1139264/Draft_Sustainability_Guidance_document__.pdf

[2] Notably, if an agreement focuses on both environmental sustainability and other social objectives, the CMA will try to determine the 'centre of gravity' of the agreement to decide if the cooperation falls within the scope of the more flexible approach provided by the Draft Guidance.

will not have an appreciably adverse effect on competition;[3]

b) concern a joint environmental initiative which could not be done by one party individually because, say, each party on their own lacks the technical expertise, resources or capabilities to undertake the initiative;

c) relate to cooperations which are required by law;

d) pool sustainability-related information about customers or suppliers (provided that no competitively sensitive information is shared and provided the parties are not required to purchase or refrain from purchasing from particular suppliers); and

e) create applicable industry standards on sustainability.[4]

2. Agreements which could infringe the Chapter I prohibition

The Draft Guidance highlights the distinction between an infringement of competition "by object" (where the effects of the breach are automatically assumed to be harmful given the egregiousness of the misconduct) and "by effect" (where harm must be shown).[5]

ESAs that are likely to have the "object" of restricting competition are those that involve any price fixing, market or customer sharing, as well as limitations of output, quality or innovation. If an ESA contains a "by object" restriction, it is still possible for it to benefit from an individual exemption – however, parties should be aware that they will face a higher bar in demonstrating that the individual exemption criteria are fulfilled.

The Draft Guidance makes a helpful distinction between competing purchasers agreeing to only purchase from sustainable suppliers where the intention is to eliminate unsustainable products from the supply chain, and agreements which are intended to eliminate a competitor, where the latter would clearly constitute an illegal collective boycott between competitors.

Additionally, the Draft Guidance also outlines that exceptions may be made where a "by object" restriction is considered to be an "ancillary restraint". A restraint will be regarded as ancillary if it is directly related and necessary to the implementation of a wider sustainability agreement that itself does not infringe the Chapter I prohibition. The wider arrangement must be impossible to carry out without the particular restraint.

Where an ESA is not a restriction by object, it will only infringe the Chapter I prohibition if it has an appreciable negative effect on competition. This effect-based assessment is fact specific depending on what the effect is (e.g. increasing prices or reducing output), and the wider context (e.g. the market coverage of the agreement, whether there is exchange of commercially sensitive information) (see also below).

3. Agreements which can benefit from an individual exemption

The Draft Guidance further explains that for all potentially anti-competitive agreements (by object and by effect infringements), it may be possible to benefit from an individual exemption under Section 9 of the Competition Act 1998, provided the four cumulative conditions are satisfied:

[4] This is provided the criteria are voluntary, transparent, reasonable and non-discriminatory. The standards must be minimum standards that businesses can exceed and businesses must be able to develop alternative standards and to sell products that fall outside the scope of the standards set.

[5] An infringement of competition "by effect" involves misconduct which is not so serious as to qualify as an infringement "by object" but which nonetheless has an appreciably negative effect on competition in the relevant market. There are a number of factors that can be considered to ascertain this, including: (i) the market coverage of the agreement; (ii) whether the businesses participating in the agreement, individually or collectively, have market power in the relevant market(s) affected by the agreement; and (iii) the extent to which the agreement constrains the freedom of action of the parties.

1) The ESA must contribute to – and the parties must be able to produce objective evidence of - benefits (i.e., improving production or distribution, or promoting technical or economic progress)

That is to say, any purported benefits need to be substantiated and cannot simply be assumed.

The Draft Guidance provides that benefits may include: (i) eliminating or reducing the harmful effects arising from the production or consumption of particular goods or services that the market has failed to address (e.g., reducing greenhouse gas emissions); (ii) improving product variety or quality (e.g., creating new or improved products which have a reduced impact on the environment); (iii) reducing production and distribution costs for a sustainable purpose; (iv) improving production or distribution processes (i.e., making them "greener"); and (v) increasing innovation (e.g., developing new, more energy-efficient processes).

Normally, business will not need to strictly quantify the benefits of the agreement if the benefits to consumers are obviously substantial. However, if the benefits are not obvious, the CMA will expect businesses to apply commonly accepted methodologies (though more bespoke methodologies will be permissible) to fulfil an evidence-based approach to quantifying the benefit.

Importantly, the Draft Guidance specifically notes that, when assessing what benefits arise from an ESA and whether consumers receive a fair share of the benefits, parties may take future benefits into account as well as, or in the absence of, benefits which may arise concurrently or soon after parties enter into an ESA. Doubtless, the CMA is recognising here that some environmental benefits can take time to be realised.

2) The ESA must be indispensable to the achievement of these benefits

In practice, this criterion may be the hardest for parties to satisfy. In order to show that restrictions of competition are indispensable (or, at least, reasonably necessary) to achieve the benefits of an ESA, parties must be able to demonstrate that, in the absence of the ESA, they would not be able to achieve the same level of benefits or else that these benefits would not be achieved as quickly.

The CMA provides a non-exhaustive list of examples of arrangements which would ordinarily give rise to a potential restriction of competition but where such restriction could be considered indispensable to achieving a sustainability objective. These include: (i) agreements between competitors to adopt a more environmentally sustainable input (e.g., an alternative to plastic) where such agreement enables these competitors to achieve economies of scale by significantly increasing the demand for the more sustainable input (through a lower final sales price); and (ii) agreements between competitors to adopt a less polluting packaging material where the higher costs involved in adopting the material by any one competitor individually (the so-called first mover disadvantage) would mean these entities would be unlikely to adopt the material without this collective agreement, the result being that the environmental benefits of the less polluting packaging material can be realised (or, at least, will materialise more quickly).

Notably, any restrictions of competition in any such ESAs must go no further than is necessary/indispensable to achieving the relevant benefits – as such, the scope and duration of the restrictions must be carefully considered.

3) Consumers must receive a fair share of the resulting benefits

Traditionally, regulators have taken a narrow interpretation as to *which* consumers can be taken into account for this assessment. Ordinarily, it is only consumers directly affected by the agreement in question that can be considered – i.e., those in the relevant market to which the agreement relates and in which the relevant companies compete. However, the CMA has clarified that, for the purposes of ESAs under the Draft Guidance, the relevant consumers can be interpreted more broadly, recognising that

environmental benefits can accrue more widely than just those in the market(s) which are directly affected. Importantly, such benefits can be accorded to consumers across multiple markets *provided that* a class of consumers are the same as, or substantially overlap with, those in the directly affected market.

4) The ESA must not eliminate competition

Parties to any such arrangement must ensure that there will be sufficient competition remaining in the relevant market in respect of a substantial part of the products/services in question. In effect, that there are sufficient players in the marketplace to continue to exert pressure on each other vis-à-vis key parameters (e.g., on price and/or quality).

Special exemption of CCAs

Parties entering into a CCA that could constitute a potential infringement of the Chapter I prohibition will largely need to employ the same self-assessment criteria as for ESAs to determine whether the arrangement could benefit from an individual exemption. However, the CMA has created a significant carve-out for CCAs.

In this regard, the CMA takes a much broader approach for CCAs than for ESAs. Indeed, the CMA has explicitly noted that with respect to the assessment as to whether consumers will receive a fair share of the resulting benefits, it is appropriate to consider the totality of benefits arising to **all UK consumers** as a result of the particular CCA in question (rather than just consumers in the market(s) affected by the CCA). The CMA explains that this is due to the "exceptional nature of the harms posed by climate change" which transcends not just those consumers in directly affected markets, but applies to wider society as a whole.

An example given in the Draft Guidance relates to a collective agreement between competitors to switch to "greener" forms of energy consumption that reduce carbon emissions. Such a measure would contribute to the UK's Net Zero targets and benefit all UK consumers, not just those which purchase the relevant competitors' products and/or services.

Proactive engagement – return of informal guidance

In another noteworthy development, the Draft Guidance provides that businesses contemplating entering into ESAs and CCAs can approach the CMA for informal guidance. In doing so, the CMA is recognising that the Draft Guidance may not be sufficient to cover all scenarios or answer all questions that may arise.

The CMA has noted that:

- Its informal assessment of the proposed arrangement will be based both on publicly available information and information shared with the CMA by the parties; and
- It is willing to indicate to businesses where proposed arrangements appear to be compliant with competition law and (where appropriate) amendments that should be made to bring these proposed arrangements into line with the competition rules. The CMA will expect the relevant parties to implement any necessary changes before any such agreement is put into effect.

Any businesses wishing to contact the CMA for informal guidance should contact sustainabilitytaskforce@cma.gov.uk. The CMA's expectation is that any request for informal guidance should be made at an early stage, but only when the parties in question have carried out an initial self-assessment.

Implications for enforcement and fines

Interestingly, the CMA has stated that:

- It will **not** take enforcement action against any ESAs and/or CCAs which closely correspond to examples the CMA has provided in the Draft Guidance; and
- It will not impose fines on any parties that sought informal guidance from the CMA in respect of any ESA and/or CCA which raised no antitrust

concerns or where concerns were addressed. This is conditioned on the requirement that parties to any such agreement must not withhold any material information when they request informal guidance from the CMA.

Next steps

Interested parties now have until 11 April 2023 to comment on the Draft Guidance – the consultation document and accompanying list of questions posed by the CMA may be accessed here. The CMA intends this Draft Guidance, once finalised, to form part of the CMA's Guidance on Horizontal Agreements (which is currently in draft form).

Final comments

The interaction between traditional competition laws and sustainability initiatives has become a fraught battleground. Regulators and policymakers alike are recognising that competition laws need to be adapted in this area to enable companies to move away from operational structures which involve a heavy carbon footprint as this shift will, in turn, allow wider society to transition away from ways of living which sustain (among other things) fossil fuel consumption and high levels of carbon gas emissions at all levels of the supply chain.

The Draft Guidance represents the first concrete indications of the CMA's future approach in this area. Currently, the welcome signs are that the CMA will look to take a flexible and relatively permissive approach, joining the ranks of the Authority for Consumers and Markets in the Netherlands, which has equally taken a more permissive stance on sustainability collaborations when compared to, say, the European Commission ("**Commission**")[6]. There are a number of areas in which the CMA's Draft Guidance goes further than the Commission's revised draft Horizontal Guidelines (published in March 2022);[7] in particular, the confirmation by the CMA that future (as well as current) benefits will be relevant to any assessment and that a broader interpretation of relevant customers/consumers is required. Moreover, the CMA has expressly stated that it will be willing to assess benefits arising to all UK consumers as a result of CCAs, not just those consumers affected directly by the arrangement, in stark contrast to the approach indicated to date by the Commission. It is expected that the final version of the Commission's guidance will be published in the coming months, this will further clarify the degree of contrast between the CMA's and Commission's respective approaches.

Looking further afield, the Australian Competition and Consumer Commission ("**ACCC**") has recently created a sustainability task force and announced an investigation into potentially 'greenwashing' businesses. The ACCC has indicated that it will take an evidence-based approach to confirm if businesses are fulfilling claims of environmental credibility[8]. Furthermore, the Philippine Competition Commission is creating a procedure to enable businesses to apply for rulings on whether agreements comply with competition law and has stated that sustainable development will form part of their considerations. Japan's Fair Trade Commission is at a similar stage to European authorities and has now drafted guidelines on the interplay between achieving ESG goals and mitigating competition risks[9]. The US however appears to be taking a less proactive approach, though the Biden administration has identified ESG objectives as a more general

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[6] Autoriteit Consument & Markt. *Guidelines Sustainability agreements, Opportunities within competition law.* 26 January 2021. Available at:https://www.acm.nl/sites/default/files/documents/second-draft-version-guidelines-on-sustainability-agreements-oppurtunities-within-competition-law.pdf

[7] European Commission. *Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (Draft)* ("**Horizontal Guidelines**"). 1 March 2022. Available at: https://competition-policy.ec.europa.eu/public-consultations/2022-hbers_en

[8] Australian Competition and Consumer Commission. *Competition and consumer issues in essential services, sustainability among 2023-2024 compliance and enforcement priorities.* 7 March 2023. Available at: https://www.accc.gov.au/media-release/competition-and-consumer-issues-in-essential-services-sustainability-among-2023-24-compliance-and-enforcement-priorities

[9] Japan Fair Trade Commission. *Guidelines Concerning the Activities of Enterprises, etc. Toward the Realization of a Green Society under the Antimonopoly Act*. 13 January 2023. Available at: https://www.jftc.go.jp/en/pressreleases/yearly-2023/January/230118EN3.pdf

Priority.[10] The variety of approaches demonstrates the importance of businesses remaining wary to potentially divergent competition regimes when conducting international cooperation on sustainability.

Returning to the UK, this specific relaxation of the applicable rules should not be taken as an opportunity by companies to implement sustainability collaborations which mask underlying anti-competitive conduct. The CMA, and other regulators, are becoming more aggressive in their enforcement and will not shy away from taking action in such instances. Indeed, if the CMA's investigation into false greenwashing claims is any indicator,[11] the CMA may in fact be still more rigorous in this area given the importance of sustainability initiatives to wider society.

It will be interesting indeed to see how this area continues to develop and how much, if at all, the CMA ultimately revises the Draft Guidance after the consultation concludes. Indeed, it must be remembered that the Commission's Horizontal Guidelines, like the Draft Guidance, have not yet been fully finalised (and are currently subject to public consultation). As such, it may be that the Commission's current position alters in due course. Stay tuned for further developments…

Contact us

Should you have any queries or wish to discuss any matter in this briefing, please do not hesitate to contact the Competition Team.

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[10] Wall Street Journal. *ESG Won't Stop the FTC*. 21 December 2022. Available at: https://www.wsj.com/articles/esg-wont-stop-the-ftc-competition-merger-lina-khan-social-economic-promises-court-11671637135

[11] https://www.shlegal.com/insights/cma-expands-its-action-against-greenwashing