

4. Formal relationships between suppliers and retailers in the UK

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Suppliers' agreements with retailers

4.1. The EC Commission has exempted the selective distribution arrangements for luxury cosmetic products (including fine fragrances) of two companies, YSL Parfums and Parfums Givenchy, from the application of Article 85(1) of the Treaty of Rome (see paragraph 3.64). In announcing its Decisions in these two cases, the EC Commission made it clear that the principles and criteria by which it had arrived at them would be the basis for deciding on similar luxury perfumery goods cases. This does not mean, however, that all agreements between the suppliers of luxury cosmetics products and their authorized retailers, and the retailer admission criteria adopted by the various fragrance houses, have been standardized, or will have to be standardized.

4.2. YSL Parfums and Parfums Givenchy, having received indications from the EC Commission that it would not introduce block exemptions under Article 85(3) for the selective distribution agreements in this industry, decided to apply for individual exemptions because their agreements did not fit the block exemptions within the terms of either EC Commission Regulation 1983/83, concerning exclusive distribution agreements, or 1984/83, concerning exclusive purchasing agreements (both of 22 June 1983). It appears that while a number of criteria are common to these two Regulations and to the YSL Parfums and Parfums Givenchy systems (eg requirements on retailers to stock representative ranges, to buy minimum quantities and to engage in promotion, and a prohibition on suppliers setting retail prices), the main focuses are rather different. The more important elements of the YSL Parfums and Parfums Givenchy systems are the qualitative criteria and the procedure for admission to the selective distribution system. In the case of the 1983/83 and 1984/83 Regulations, territorial issues (absent from the YSL Parfums and Parfums Givenchy agreements) are a major concern. Furthermore, the Parfums Givenchy agreement requires that retailers stock competing products, while the 1983/83 and 1984/83 Regulations allow agreements to prohibit dealers from distributing competing goods.

4.3. The Decisions by the EC Commission give complete exemption to the YSL Parfums and Parfums Givenchy 'standard-form authorized retailer contracts'. The exemptions became applicable on 1 June 1991 in the case of YSL Parfums and on 1 January 1992 in the case of Parfums Givenchy, and remain so until 31 May 1997 in both cases. The EC Commission has indicated its intention to re-examine two aspects of the exemptions in particular at the end of this period:

- (a) the minimum annual purchases requirement; and
- (b) the duration of the admission procedure.

In the meantime YSL Parfums and Parfums Givenchy were each required (on 1 June in the years 1993, 1995 and 1997) to provide the EC Commission with the following information:

- total purchases of YSL/Givenchy products achieved (during each of the previous years) by all the authorized retail outlets in each member state of the EC, any increases made in prices, and the launching of new products or the withdrawal from the market of old products;
- the number of authorized retail outlets in each member state as at 31 December in each of the previous years; and
- the minimum annual purchase amounts set annually by YSL/Givenchy or (where appropriate) by their exclusive agents, for their authorized retailers.

4.4. A number of other suppliers have recently modified, or are in the process of modifying, their retailer supply agreements to make them consistent with the Decisions, and have formally notified their new agreements to the EC Commission with a view to receiving letters of comfort, in regard to their acceptability under Article 85. Several suppliers told us, however, that the changes that had been, or were likely to be, made were not very far-reaching compared with their previous policies. One of the fragrance houses, Parfums Rochas SA (Parfums Rochas), told us that it wanted its agreement to differ from the YSL/Givenchy pattern (particularly in that it wanted its French agreement, but not the UK one, to provide for a waiting list of retailers seeking authorization) and that it had sought what was termed a 'negative attestation' or, in case of a refusal from the EC Commission, an exemption on the basis of Article 85(3) of the Treaty, or alternatively a *lettre de classement*. However, Parfums Rochas told us that it did not expect to receive any response from the EC Commission while three cases appealing against the YSL Parfums and Parfums Givenchy Decisions were pending before the EC Court of First Instance.¹

4.5. The contractual relations between a number of the suppliers and their retailers in the UK, as well as in other EC countries, are therefore currently undergoing a process of change. While we analysed in some detail the old and the new agreements where they existed, and our findings are summarized below, it was not practicable to record comprehensively every change in these formal arrangements. We noted, too, that while a number of the suppliers are now signing up their UK retailers to the new agreements, some retailers had not yet decided to sign. Most of the suppliers told us that they would eventually have to cease supplying any retailers, even large ones, which refused to sign the new agreements.

4.6. The key features of the YSL Parfums and Parfums Givenchy systems are as follows:

- all purely quantitative criteria for limiting the numbers of retailers admitted to the network are eliminated;
- a procedure is introduced for the automatic admission of new retailers, subject only to the application of certain qualitative criteria and a delay of not more than 12 months;
- retailers must meet certain specific and objective qualitative criteria for both staff and premises if they are to be admitted to the system;
- any retailer which meets these criteria and is willing to accept the obligations in the retailer agreement will be admitted to the system;
- authorized retailers must meet minimum annual purchase requirements, carry a minimum range of stock, and undertake various promotion and advertising activities;

¹The three cases are: (a) *Groupement d'Achat Edouard Leclerc [of Paris] v Commission of the European Communities* (Case T-19/92) brought on 9 March 1992 (which requests that the Court annul the EC Commission's decision on the YSL Parfums case on the grounds that, among other things, it was based on an inadequate analysis and understanding of the market and of consumers); (b) *Groupement d'Achat Edouard Leclerc [of Paris] v Commission of the European Communities* (case T-88/92) brought on 21 October 1992 (which requests that the Court annul the EC Commission's decision on the Parfums Givenchy case on similar grounds); and (c) *Kruudvat BVBA [of Sint-Niklaas, Belgium] v the Commission of the European Communities* (case T-87/92) brought on 19 October 1992 (which requests that the Court declare void the EC Commission's Decision on the Parfums Givenchy case on similar grounds).

- subject to the above, retailers are free to decide which luxury perfume brands and products they wish to sell alongside each other;
- authorized retailers must obtain their supplies from authorized distributors or other authorized retailers, and may only sell to consumers on or from their premises or to other authorized retailers whether in their own country or elsewhere in the EC; and
- it is clearly stated that retailers are free to set their own retail prices.

4.7. Among the fine fragrance suppliers in the UK, nine (including YSL and Givenchy) include in their agreements the bulk (ie between 10 and 14) of the 15 clauses exempted by the EC Decisions (these are listed in Table 4.2). These nine are all currently using retailer contracts which have been drawn up taking into account the YSL Parfums and Parfums Givenchy Decisions. Another five suppliers, each planning to introduce a new agreement consistent with the EC Decisions, include between four and nine of the provisions in their existing agreements. Four of the suppliers include between one and three of these provisions, and ten suppliers currently do not have a contract which contains any of the exempted clauses. Table 4.1 summarizes the situation for the different companies.

TABLE 4.1 Summary of types of retailer agreements in use and proposed

Already using agreements based on the YSL Parfums and Parfums Givenchy exemptions

Chanel Givenchy PAL
Dior Klein P&C
Giorgio Lauder* YSL

Using some form of agreement and/or terms and conditions of sale but planning broadly to change to the YSL Parfums and Parfums Givenchy systems

Arden Hermès§ Procter & Gamble
Alfred Dunhill† Lancaster Ricci
Golden Parim Sanofi
Guerlain‡

No agreement or terms and conditions of sale but planning broadly to introduce YSL Parfums and Parfums Givenchy systems

Douek Patou

Using terms and conditions of sale; no significant change proposed

Green¶ Revlon Shiseido
Muelhens

No agreement/terms and conditions of sale (other than those relating to each individual order) and none proposed

Creative Fragrances⌘ Diana de Silva Houbigant

Source: MMC, based on an analysis of information from the companies.

*Lauder finalized its new pan-EC store agreement in January 1993, and began signing up retailers in the UK in June 1993.

†Changes will take account of the outcome of the MMC inquiry; no specific mention of the YSL Parfums or Parfums Givenchy Decisions.

‡Guerlain said that while it was planning to change to an agreement which bore a similarity to the YSL Parfums and Parfums Givenchy agreements, and in so doing (where appropriate) taking account of the principles contained therein, it did not consciously seek to identify with those agreements.

§Changes were being made to its French agreement. Any consequential changes to the UK agreement were unlikely before 1994.

¶Green, a new company, was awaiting retailers' contracts from its principal supplier companies in Paris.

⌘Parfums Rochas (whose wholly-owned subsidiary in the UK, Rochas Perfumes Ltd (Rochas), is its representative on the UK market through the assistance (*prestataire de services*) of Creative Fragrances) has notified its standard authorized retailer agreement to the EC Commission, and is awaiting a response.

4.8. The provisions exempted in the cases of YSL Parfums and Parfums Givenchy which appear to be most important from a competition point of view are summarized in Table 4.2. They include a number of basically quantitative provisions (eg minimum annual purchases and certain limitations on the acquisition and sale of the products) which are subject to Article 85(1) but which have been exempted under Article 85(3), and other provisions of a qualitative nature. These provisions are all listed in full in Appendix 4.1 (this appendix summarizes the contents of the agreements for only those companies which we found to be part of the complex monopoly). In preparing this analysis we examined the formal retailer agreements (and conditions of sale where appropriate) provided in time by 28 suppliers of fine fragrances to the UK market. (It should be noted that the absence of a 'tick' in Appendix 4.1 in respect of those companies which do not have formal supply agreements may not necessarily mean that the company concerned does not apply the relevant provisions, because some are included in miscellaneous other documents such as distribution policy letters, etc.)

TABLE 4.2 Summary of clauses in the exempted YSL Parfums and Parfums Givenchy authorized retailer contracts which are important from a competition point of view, and the frequency of their occurrence in UK suppliers' contracts with retailers

<i>Clause*</i>	<i>Frequency†</i>
I.i.a Recognized qualification/experience	9
I.i.b Training	8
I.ii Location, name and fittings of outlet	10
I.iii Prohibition of sale of other goods which might detract from image	8
I.iv Sales area, including availability of competing brands	10
I.v Selling requirements: sales permitted from authorized premises only,‡ original packaging to be retained	13
I.vi Stocks: quantity and freshness	12
I.vii Promotion and advertising, including stocking new products	12
I.viii Minimum annual purchases	9
II.i Admission procedure: application followed by inspection re qualitative criteria	6
III.i Authorized retailers may resell to other authorized retailers throughout the EC	15
IV.i Authorized retailers will not sell to or obtain supplies from any wholesaler or retailer not included in supplier's distribution network	15
V No imposed prices	9
VI Competing products may be purchased	-
VII.i Term and renewal of contracts	11

Source: As Table 4.1.

*The YSL Parfums and Parfums Givenchy exemptions are very similar but not identical. All exemptible clauses from either Decision are included in the list of provisions against which the agreements have been analysed. Clause numbering reflects the more detailed listing of provisions in Appendix 4.1.

†These numbers relate to a total of 28 companies. It should be remembered that a number of companies are in the process of revising their agreements, or have already said that they do not intend to introduce agreements which incorporate the principles set out by the EC Commission in its YSL Parfums and Parfums Givenchy Decisions (see Table 4.1). In the case of Lauder, the analysis in both this table and in Appendix 4.1 includes information from its British store agreement, and this was superseded in June 1993 by Lauder's new pan-EC store agreement containing provisions which were drawn up in the light of the EC Decisions on YSL Parfums and Parfums Givenchy.

‡See also paragraph 4.13.

4.9. While both Table 4.2 and Appendix 4.1 show that we did not find any explicit provision in the agreements allowing retailers to stock competing products, the absence of any provision prohibiting them from doing so implies that they can do so if they wish. Indeed, unlike the standard-form contract in the YSL Parfums Decision, that in the Parfums Givenchy Decision explicitly requires that the 'authorized retail outlet must, within eighteen months ..., carry a sufficient number of competing brands to reflect the image and reputation of Givenchy products'. This, the EC Commission explained in its Decision, was necessary in order to attract and retain the loyalty of consumers who expect to find, in each retail outlet, a specialized commercial environment allowing them to choose from a range of competing brands. In satisfying this condition, retailers are free to choose which brands to stock (provided only that they are brands of luxury cosmetic products which are usually distributed through selective distribution networks). In the EC Commission's view, as expressed in the Parfums Givenchy Decision, the minimum number of four competing brands, in addition to the supplier's brand(s), imposed by Parfums Givenchy up until the Decision, was 'not unduly high, given the degree of specialization that is currently a usual feature of the distribution of luxury products' in the EC.

4.10. Again, while only nine agreements expressly stated that authorized retailers are free to set the resale prices of their products, all suppliers indicated, in response to a question in our questionnaire, that this was the case. On both this point and that in paragraph 4.9, some suppliers told us that when the opportunity arose (eg when reprinting their documentation) they would be modifying their agreements to make these two points more clearly.

4.11. On a related point, there was no sign in the agreements that the legal opinion in the YSL Parfums and Parfums Givenchy Decisions that 'the down-market nature of a retail outlet or of its name cannot be deduced from the retailer's habitual policy on prices' was being disregarded (though see paragraph 7.129, where we note that a suggestion to this effect was included in Lancôme's draft evaluation report for assessing the suitability of new retail outlets). Several agreements (eg Givenchy, Dior, Jean Patou Limited (Patou)) expressly stated that the normal pricing policy followed by a retailer should not be considered as a prestige- or value-reducing factor.

4.12. We discussed particular points arising from their individual retailer agreements with a number of the companies. For example, the agreements of two suppliers (namely YSL and P&C) stated that if an authorized retailer decided to transfer the point of sale and thus to change the location from which the products were sold, it should be able, once the transfer had taken place, to obtain the authorization of the exclusive distributor for the new point of sale subject to a number of conditions, of which one was that: 'The new point of sale must be located in the same town, and if the town is divided into districts, in the same district as the point of sale which has been closed or in the surrounding districts.' This seemed to be a territorial restriction not covered in the exemptions and could in certain circumstances have the effect of territorial exclusivity. YSL told us that rather than being an additional restriction, this was a limited exception to the conditions in that it enabled an existing retailer to move premises locally without having to go through the full evaluation routine for new outlets (which might involve a wait of up to nine months before obtaining new supplies). P&C similarly regarded this as a more relaxed rather than a tighter restriction, but anyway said that the relevant clause in its standard agreement was no longer applied and that this was mentioned in the covering letter sent out with the agreement.

4.13. One of the differences between the YSL Parfums and Parfums Givenchy contracts assessed in the EC Decisions is the treatment of mail order sales. The YSL Parfums contract states that authorized retailers 'must display and sell Yves Saint Laurent products only on the premises covered by the contracts and must refrain in particular from selling them by mail order'. The Parfums Givenchy contract states that authorized retailers 'must display and sell Givenchy products solely on the premises covered by the contract'. We questioned a number of the fragrance houses about whether they considered that these provisions meant that fine fragrances could only be sold to customers during their visits to authorized retail outlets. We were told that customers could order fine fragrance products by telephone or mail and receive them in postal deliveries, provided that the orders were placed directly with, and processed by, authorized retail outlets where qualified and experienced consultants were available to handle customer queries at the time of ordering.

4.14. Having noted that Dior's agreement specifically states that the retailer 'undertakes not to resort to mail order, catalogue sales, or any sale or order or delivery of products outside the point of sale', we questioned the company about what this meant in practice given that we had been shown a copy of a 1991 Harrods mail order advertisement specifically for several Dior perfumes leading with its (then) newly launched Dune brand. (Harrods runs such mail order advertisements in the national press for other brands too.) Dior told us that while in principle mail order sales were not permitted, Harrods' mail order activities were seen as an extension of customer service to its existing customers, and that the wording of its contract needed clarifying in this respect.

4.15. While some suppliers said that in determining the suitability of new retailers they did not discriminate in favour of or against any particular category of retailer (and some maintained that their admission criteria now applied consistently to different types of outlet throughout the EC), we also noted that several indicated in their answers to our questions that they were only interested in allowing certain categories of retailer into their selective distribution network. For example, Guerlain told us that the primary criterion for deciding on whether to supply a particular company with reference products was whether the retailer was a department store, retail pharmacy, perfumery or beauty salon. If not, it was not accepted. While Lauder stated that its authorized sales outlets would be either prestigious retailing units or within the

perfumery section of a department or speciality store, it also said that its new criteria for assessing potential new entrants to its selective distribution network would apply consistently to different types of outlets throughout the EC, including supermarkets, and that some supermarkets might be sufficiently prestigious to qualify for selection under its criteria. See also the reference to Muelhens' policy in paragraph 4.23.

4.16. A number of companies (including P&C, Klein, Lauder, Lancaster, Sanofi, Revlon, Muelhens, Diana de Silva and Creative Fragrances) indicated that they regularly or occasionally had temporary exclusive launches (over a period of anything from around three weeks to one year) of their products in one or more stores. Only one of these companies, P&C, also has a clause in its agreement which states that authorized distributors shall stock all new brands of the products launched by it from the date of launch in the UK. In P&C's view, this ensured that consumers could be certain that they could sample and buy new brands launched in the UK, and that both the supplier and the retailer derived maximum benefit from the advertising and promotional expenditure in support of the new brand. This, P&C said, was consistent both with the EC Commission Decisions on YSL Parfums and Parfums Givenchy, which accepted generally that retailer co-operation in advertising and promotional activities was important in ensuring their success, and with the view set out in the Parfums Givenchy Decision that the successful launch of a new luxury cosmetic product 'presupposes close cooperation between the manufacturer and its authorized retailers, who, for their part, require specific training in order to provide final customers with the professional advice they expect'.

4.17. We noted that the Dior agreement states that: 'no food or household products may be sold at the point of sale, or, in the case of department stores or multi-purpose stores, within 50 feet of the perfumery and beauty department and/or visible therefrom'. As it may seem that if taken literally, not only Boots, but possibly also department stores like Harrods, would fail to meet this criterion, we asked the company to explain what this restriction meant in practice. Dior said that while Boots did sell sandwiches (mostly in its London outlets), this was a very minor part of its business and did not detract from the very high image and authority that Boots had in the beauty and healthcare markets; similarly in the case of Harrods, whose very high reputation in the sale of cosmetics and perfumery was not debased in any way by its food hall. This would all be in contrast to stores such as Tesco, where food sales predominated.

Criteria for admitting new retailers

4.18. The first part of this chapter examined retailer agreements and related documentation of 26 suppliers of fine fragrances to the UK market. We now turn to the criteria used by the suppliers to determine whether or not a particular retail outlet appears to them to be suitable premises from which consumers should buy fine fragrances. For this purpose many suppliers have now put together check-lists which set out a number of criteria to be assessed and scored. We reviewed these retailer check-lists and compared them with the selection criteria in the retailer agreements. We also looked at the suppliers' responses to a number of questions that we put to them about the selection of retailers. Our findings are summarized below and in Appendix 4.2.

4.19. Ten companies used some form of check-list, and we found that all these, except Muelhens', were in line with the EC criteria. A further six companies indicated that they were already drafting, or intended to introduce, a check-list (Arden, Guerlain, Patou, Maurice Douek Limited (Douek), Ricci and Sanofi). Ten suppliers did not use, and were not planning to use, a check-list. Apart from Muelhens (which does not have a formal retailer supply agreement against which to compare the provisions of its check-list), the check-lists were broadly consistent with the criteria contained in the retailer agreements in terms of headings and matters covered, although the check-lists were often considerably more detailed than might have been expected. We found a considerable variation in the number of questions included in the check-lists: for example, while Givenchy's has 15 (scored) questions, Chanel's has 45.

4.20. All but one of the check-lists (that of Muelhens-see paragraph 4.23) used some form of point-scoring system, including an overall minimum score (and sometimes also a minimum score for certain subsets of questions) which the outlet must achieve in order to join the supplier's selective distribution network. In about three-quarters of cases, the suppliers automatically eliminate applicants scoring the minimum point in the range for several key questions. In addition to scored questions most check-lists also included a number of additional questions which were not explicitly scored. The influence of the answers to these questions on the final decision as to whether or not to supply reference products to an applicant was not always clear.

4.21. In addition, many companies required a number of photographs (up to 14 or 15) of various aspects of the store environment, exterior, interior and staff. The selection criteria are usually made known to the applicant (including several cases where no check-list was used), mostly prior to evaluation. We found that the final decision as to whether or not to admit a new retail outlet was most commonly in the hands of the Sales Director but there were quite a few variations on this. A number of suppliers mentioned referring to the Managing Director in difficult cases. The letters to unsuccessful applicants usually highlighted features of the store which were given low scores.

4.22. We found that the check-lists varied greatly in detail and complexity, and that a few were difficult to follow at first sight. Nearly all the suppliers used the same check-lists for all types of outlet. However, when using their check-lists to assess pharmacy or perfumery outlets, rather than department stores and other outlets where there are one or more dominant activities other than the sale of perfumery products, a few suppliers miss out several of the questions. Only Dior used two separate check-lists for chemists and department stores. Dior also used an additional questionnaire in situations where the shop was located in an arcade/shopping centre.

4.23. Muelhens described its account opening process as follows. First, its strategy was to have no more than 200 to 300 outlets, confining distribution to department stores and very top quality perfumeries. Second, the selected accounts to be opened were individually known by its (Muelhens') management team, including the positioning in town, its neighbourhood, the retail offer, the quality and training of the staff, the quality of the environment, and whether a broad selection of competitive brands were stocked. Third, a site visit was undertaken to check whether the outlet met Muelhens' documented account-opening criteria, and an assessment would be made during the visit to see whether or not it would be profitable for Muelhens to open the account. This selection process, Muelhens said, followed the arrangements approved in the YSL Parfums and Parfums Givenchy Decisions.

4.24. A number of the suppliers provided us with examples of completed check-lists for both successful and unsuccessful applicants. In these cases, the assessments appeared to have been carried out even-handedly. However, it is difficult to challenge the scoring in any given case without good photographs and, preferably, a site visit.

4.25. The suppliers claimed to achieve consistency in applying the criteria in a variety of ways—sometimes by several ways in combination. The most commonly cited means was having the final decision taken by one and the same person. Having a standard check-list and/or standard criteria was also cited. Other methods included having all the area representatives visit a similar mix of retail types, various types of training, briefing and guidelines, and spot checks. Only YSL had a single representative visiting all applicants (see paragraph 4.26). Klein had only four representatives, and several suppliers (eg Patou and Douek) which were introducing new systems in the future also intended having only one inspector.

4.26. YSL told us that when its standard authorized retailer agreement was first introduced in the UK, evaluations were carried out by area managers, each of whom was responsible for a different part of the UK. Although the evaluators used standard check-lists and were given training prior to beginning their evaluations, comparison of the evaluations carried out in the early months indicated that the criteria were not being applied consistently by the different evaluators. YSL had now appointed a single evaluator, and was undertaking a reappraisal of all outlets.

4.27. P&C, too, told us that it had found, during the course of responding to our questionnaire, that its admission policy had not, on a number of occasions in 1992, been applied correctly. P&C said it had found that despite the fact that some point-of-sale evaluation reports indicated that the retailers concerned stocked grey-market supplies of P&C's competitors' brands, the applications had been approved without further investigation. As well as requiring the assessor to show for each major fine fragrance brand currently in stock whether it was obtained from official or from unofficial (ie grey-market) sources, P&C's check-list contains a question on alternative or copy fragrances, but none of these are scored and they are not in themselves eliminating factors. P&C told us that while it would not admit a retailer which continued to sell unofficial P&C products, it might or might not refuse to supply retailers which continued to stock unofficial supplies of other suppliers' brands, depending on the quality of the outlet's presentation of fine fragrances generally.

4.28. It is perhaps inevitable that there are some teething problems in the introduction by the various fragrance houses of these new agreements and the corresponding retailer check-lists. Even so, given the extent of judgment involved in assessing many of the individual criteria it is not clear whether it could ever be guaranteed that they could be applied even-handedly either across a variety of retail categories at any moment in time or, more generally, over time as the assessing personnel change, standards change in the design and fitting out of retail outlets, and the general public's expectations about the quality and service standards they can expect from the various categories of retailer evolve.

The Verdict Research survey

4.29. In January 1993 we commissioned Verdict Research Limited (Verdict), an experienced firm of retail analysts and consultants, to undertake a field survey of fine fragrance retailers (the Verdict report). Verdict visited 101 retail outlets selling fine fragrance products, evaluated each using a check-list (see paragraph 4.30), and prepared an audit of the range of physical and other conditions under which fine fragrance products were sold in the UK during February 1993. As the Verdict report was intended to cover a wide range of outlets selling fine fragrances, and as consumers are not necessarily aware of the distinction between authorized and unauthorized retailers, no attempt was made either during the survey or in the formal presentation of the results to distinguish between authorized and unauthorized outlets. However, Verdict estimated (based on the fine fragrance presentation in the store and the extent of point-of-sale support from authorized distributors) that 33 of the outlets it visited were unauthorized (including the Asda, Superdrug, Tesco and Perfume Shop outlets, and a few of the chemists outlets), and a further seven may have been unauthorized. Relevant extracts from the Verdict report are reproduced in Appendix 4.3.

4.30. Verdict put together a pro forma check-list setting out the criteria (as shown at the end of Appendix 4.3) against which the retail outlets were to be assessed. This check-list included what Verdict considered to be the most relevant and appropriate criteria after first analysing a number of the quite diverse check-lists used by the fragrance houses for assessing potential new retailers (see paragraph 4.18). The aim was not to produce assessments which were either consistent with or in conflict with those done by the perfume houses, but to develop a check-list which could be used to evaluate a disparate range of retail outlets consistently and on a directly comparable basis. In our brief to Verdict we said that we considered it was essential that the check-list should enable the various conditions found in retail outlets to be compared, the range of conditions readily summarized and assessed, and that the scoring system should be applied objectively and even-handedly as between all types of retail outlet encountered.

4.31. The qualifications and training of consultants was handled separately, and during the visits that Verdict made to the retail outlets it surveyed, brief questionnaires were left for the perfume counter staff to complete and return to the MMC (this approach was agreed between Verdict and the MMC because it was thought that beauty consultants would not readily provide personal information about themselves to Verdict's field staff). The questionnaire asked about the respondent's length of experience, and types of training and other qualifications. The MMC received 312 completed questionnaires from 43 different retail outlets (an average of 7.3 questionnaires per outlet).

4.32. In analysing these results, scores were allocated to each retail outlet according to the consultants' length of work experience and the type of training (the scores covered all consultants, and did not distinguish between those consultants employed by the retailer and those employed by the perfume houses). Possible total scores for each individual store ranged from 2 (the minimum score) to 25 (the maximum score). The scores in fact ranged from 4 to 19, with a mean score of 11.2, and a mode of 13. Almost two-thirds of the stores achieved a score in the range 10 to 13. The three highest scores (19, 18 and 17) were achieved by stores in two multiple department store chains, and the lowest score (4 points) was achieved by two supermarket outlets. The five Superdrug stores (out of seven visited) which provided completed questionnaires achieved scores in the range 7 to 12, with an average of 10.4.

4.33. As Table 1 in Appendix 4.3 shows, Verdict's scores in the main survey ranged widely from 94 (being 97 per cent of a possible maximum score of 97) for the Debenhams department store in Leicester to 37 (being 45 per cent of a possible maximum score of 82) for the Asda supermarket in Nottingham. The mean score for all the outlets was 69 per cent. For the 33 outlets identified by Verdict as being unauthorized, the mean score was 60 per cent (the range being from 78 per cent each for three Perfume Shop outlets and a Superdrug outlet, to 42 per cent for an independent chemist). The score achieved by the lowest rated authorized outlet in the survey appears to have been 53 per cent, for an independent department store.

4.34. Among the different categories of retailers, the highest-scoring category was airport duty-free shops (with a mean score of 85 per cent), and the lowest were independent chemists (56 per cent) and supermarkets (54 per cent): see Table 4.3. Verdict noted some considerable variations in the quality of presentation within some of these categories. For example, the main department store category (which encompassed 32 stores) included both the highest-rated outlet in the survey (with a score of 97 per cent) and two stores each with scores of 57 per cent. In the multiple chemists category (with 17 stores) there were five stores each with scores of 80 per cent or more, and two stores with scores of 58 per cent and 49 per cent respectively.

TABLE 4.3 Verdict survey results showing outlet scores by category of retailer

<i>Category of retailer</i>	<i>Score*</i>
	<i>%</i>
Duty-free shops at airports	85
Perfume specialists†	78
Department store groups	75
Drugstores‡	72
Multiple chemists shops	71
Independent department stores	67
Independent chemists	56
Supermarkets	54
Average score for all outlets	69

Source: MMC, based on Verdict survey results.

*Scores as a percentage of the maximum possible score for the respective categories.

†That is, four Perfume Shop outlets.

‡That is, seven upgraded Superdrug outlets.

4.35. The range in quality already noted was also seen even for different stores under the same ownership. For example, the scores for the five Alders department stores ranged from 93 per cent down to 61 per cent. Scores for the seven Lloyds Chemists plc (Lloyds) outlets surveyed ranged from 82 per cent down to 49 per cent. The scores given to the ten Boots stores that Verdict visited ranged from 85 per cent down to 65 per cent, and the HoF stores' scores ranged from 88 per cent down to 60 per cent.

4.36. Among known unauthorized retailers, the seven Asda stores selling fine fragrances which Verdict visited were given scores ranging from 60 to 45 per cent, and the seven Tesco stores ranged from 63 to 48 per cent. Verdict also visited seven Superdrug stores selling fine fragrances, and gave these scores ranging from 78 per cent down to 67 per cent. Of four outlets of the Perfume Shop—a small chain of specialist perfumeries which at the time of our survey was selling fine fragrances, obtained entirely from grey-market sources, at discounted prices—one scored 77 per cent and the other three 78 per cent each.

4.37. Though not part of its brief, Verdict suggested that, as a rough guide, 60 per cent might be regarded as a pass mark. Any individual fragrance house using Verdict's check-list (as discussed earlier in this chapter, the houses have their individual check-lists which differ both from each other and from Verdict's) might, of course, choose a different pass mark depending on the particular standards it wished to see achieved. However, if 60 per cent is taken to be the pass mark, each of the seven Superdrug outlets would have passed, as would four of the 14 supermarket outlets (three of Tesco's and one of Asda's). More generally, 22 of the 101 outlets surveyed by Verdict were given scores of less than 60 per cent and of these, ten were supermarkets, seven were independent chemists, three were authorized department stores and two were outlets of a multiple chemist (Lloyds). Givenchy told us that 62 of the 101 outlets were among its

authorized stockists, including only three of the ten independent chemists surveyed. Of the 62, four were scored by Verdict below 60 per cent. YSL noted that its authorized retailers had generally scored very well in the Verdict survey, and commented that the few that had not (being among those which had not yet been re-evaluated by YSL using its new check-list) might well be among those which YSL would have to cease supplying.

4.38. As an extension of the main survey, we also asked Verdict to visit a number of retail outlets which we knew had applied for, and been refused, authorized status by one or more of the perfume houses. Of these, Verdict found that a number were no longer trading, or perhaps had never begun to trade having made an unsuccessful approach to one or more of the perfume houses. However, Verdict was able to visit 18 stores whose applications had been refused by one or more of the perfume houses. The resulting scores are shown at the end of Table 1 in Appendix 4.3. The scores ranged from 78 per cent (for a beauty salon in Leeds which was an authorized stockist for many of the perfume houses but which in 1991 had been refused supplies by one of the main fragrance houses) to 37 per cent (for an independent drugstore in London). Twelve of the 18 stores visited were independent chemists shops, and these were given scores ranging from 65 per cent down to 40 per cent. Verdict noted that independent chemists were usually small businesses with limited resources, often located in neighbourhood settings or in secondary high streets. The scores given reflected these limitations. One Tesco supermarket and one Superdrug store were also visited as part of this additional survey, and each scored over 60 per cent (the Tesco store at New Malden was rated at 63 per cent, and the Superdrug store in the Epsom shopping centre was rated at 76 per cent).

4.39. We showed the results of the main Verdict survey, and the results of the subsequent analysis of consultants' experience and training, to the main fragrance houses. We also showed the survey methods and the particular results for their outlets to some of the main retailers mentioned in the survey. The comments on the Verdict report varied a good deal. Some criticized it extensively, while others considered that, given the nature of the task, Verdict's report was a sound piece of work and in some cases accorded fairly closely with their own evaluation approach. Many of the suppliers pointed out that Verdict had not taken account of the shop name, or *enseigne*, which they regarded as an essential criterion. The Verdict survey, it should be noted, was intended simply as a physical audit of retail outlets selling fine fragrances, and the scoring system was specifically designed by Verdict to avoid any prejudices that might arise if consideration was given to the type of outlet or the shop name.

4.40. Among other comments made to us were the following:

- Verdict omitted a number of criteria which were permitted in the EC exemption Decisions and which were important, eg height of display cabinets and length of windows;
- on the other hand Verdict included one factor, parking, which most suppliers did not include and regarded as irrelevant;
- Verdict had evaluated some aspects in a broad way (eg condition of decoration, whereas the supplier check-list specified the date of last redecoration) and so entailed greater subjectivity (Verdict commented that that in the context of its survey finding out the date of a store's last decoration would have been very time-consuming);
- Verdict appeared to place undue emphasis on the newness of the shop or its fittings;
- some of the individual outlet scores were thought to be difficult to reconcile, eg Superdrug stores scoring ahead of John Lewis's Peter Jones store in Sloane Square: this cast some doubt on the validity of the scoring system (this comment shows how easy it can be for some prejudice to enter into the assessment of retail outlets in the absence of a scoring system, such as that devised by Verdict).

The Research International postal survey

4.41. While we were readily able to obtain information and views from the major retailers of fine fragrances, eg the department stores, duty-free retailers and the multiple chemists shops, we also thought it important to find out more from a random sample of smaller retailers, all of them independent pharmacies or drugstores. We therefore commissioned RI, a specialist market research company, to conduct a postal survey for us. The relevant parts of the RI report are set out in Appendix 4.4.

4.42. The survey was carried out in February and March 1993, and involved sending questionnaires to some 3,000 independent retailers (comprising 2,750 pharmacies and 250 drugstores), these having been selected (by Nielsen Marketing Research) as a geographically representative random sample of about one in three independent pharmacies and about one in four independent drugstores. RI received 995 replies, giving a response rate of 33 per cent.

4.43. About three-quarters of those which replied said that they did sell fine fragrance products, and most had been doing so for several years. We particularly noted that the vast majority (93 per cent) of those selling fine fragrances acquired some or all of their stocks from the grey market. About one-third said that they used both grey-market and authorized suppliers, and only 6 per cent relied solely on authorized suppliers.

4.44. The main reason given by retailers for using the grey market was that their annual sales were too low to justify seeking authorized stockist status. About 71 per cent of the respondents had an average annual turnover for all products of less than £40,000, and 78 per cent had annual sales of fine fragrances of less than £10,000. A retailer having, or expecting, only a relatively modest annual turnover from fine fragrance products would not only find it very difficult to obtain authorized status simply because of the low turnover, but could also find the stock level and other obligations required of authorized retailers financially onerous (especially with a requirement to stock competing brands). Fifty respondents had applied for authorization and three-quarters of those had been turned down. The reasons given were usually that there were other authorized distributors too near their outlet or that the fragrance house was not planning to expand (it should be noted that such reasons are no longer compatible with the principles behind EC-approved selective distribution systems for fine fragrances). Thus, obtaining supplies from the grey market appeared to be the only means open to such retailers to obtain the small quantities of the stock they were able to sell.

4.45. Some 37 per cent (ie 282) of the respondents were currently authorized stockists for one or more fragrance houses. Asked how the fragrance houses responded when they first applied for authorization, 17 per cent said that they were refused without explanation, while the rest were either accepted straight away, received visits from the fragrance house and/or were asked to make changes before they could be authorized. Of those asked to make changes, 41 per cent were asked to train their existing staff to a higher standard while the other requested changes were to do with the shop's physical condition and fittings.

4.46. We sent a copy of the RI report to the main fragrance houses, and a number sent us their comments, some in considerable detail, on its findings. Some noted that the survey found that 36 per cent of authorized retailers were selling at less than RRP, and that there was no sign of other retailers being unaware of their ability to undercut recommended prices. It was also noted that opinion had been divided on whether retail gross margins were relatively high or low on fine fragrances. One supplier said that the survey results suggested that the fine fragrance market was highly competitive, with no evidence that retailer demand for fine fragrance products was not being fully satisfied. This supplier also believed that the RI survey pointed to the unwillingness on the part of unauthorized retailers to comply with suppliers' requirements as being the main barrier to authorization, rather than the fragrance houses' reluctance to grant it. Another of the main suppliers considered that as most of the respondents had probably applied for authorized status more than two years ago, before the YSL/Givenchy systems had been approved by the EC Commission, their experiences were based on the previous supply arrangements and hence some of their comments were no longer valid (eg that supply had been refused on quantitative grounds).

4.47. The suppliers' criticisms of the RI report included:

- mention of the fact that the survey had been commissioned by the MMC might have affected the response rate (in the view of one supplier, it was inevitable that respondents would be conscious of the debate surrounding the MMC inquiry, and that, being placed on notice that the survey was being undertaken within that context, respondents' replies to questions would be coloured accordingly);
- the phrasing of certain questions was insufficiently neutral, and might have affected responses;
- that it was a postal survey, and that surveys of this kind tended to draw out responses only from those with strong feelings; and
- concern about the low response rate (33 per cent), which had implications for the representativeness of some of the findings.

4.48. We showed some of the more detailed comments to RI for its reactions. It emphasized that while it was given a short time-scale in which to conduct the postal survey, it had been given a very detailed brief by the MMC and had followed the usual professional practices to ensure that, as far as possible, the survey results were representative. We recognize that postal surveys, as with other types of survey, have their potential limitations, but they are nevertheless needed as a cost-effective source of market information about relatively large numbers of respondents. We have borne in mind the various comments we received when interpreting and making use of the results of this particular survey.