

7 Views of suppliers

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Suppliers who attended hearings

Calvin Klein Cosmetics (UK) Limited

Selective distribution

7.1. Klein said that it operated a selective distribution system, as sanctioned by the EC Commission, to ensure that its products were widely available in outlets which provided suitable conditions as laid down in its criteria for retailers.

Retailers' costs

7.2. Klein did not believe that the selective distribution system resulted in retailers' costs being too high. To be successful, an authorized retailer had to provide customer service and offer an adequate number and range of products. Klein shared the costs of beauty consultants and point-of-sale fittings in special cases.

Stockholding requirements

7.3. Klein said that its business philosophy was based on the availability of a 'wardrobe' of fragranced products; consumers should be given the opportunity to purchase a range of products which complemented their fragrances. Authorized retailers were required to hold two-thirds of the items, or SKUs, in its range. Klein communicated regularly with retailers to review their sales and stock and to ensure that supplies were in balance with demand. There was an annual stock balancing, when excess products could be returned or exchanged.

Level of prices to consumers

7.4. Klein said that fine fragrance prices were not high and reflected the costs of development, manufacture, advertising, promotion and distribution. Manufacturing, wholesale and retail margins did not provide excessive profits after meeting these costs. Retail margins were lower than on some other categories of product.

Recommended resale prices

7.5. Klein pointed out that recommending resale prices was a long-standing practice in the fine fragrance industry. It allowed the supplier to set uniform wholesale prices as a percentage of the RRP. However, retailers were free to set their own retail prices. Klein did not monitor the pricing policy of its retailers and would normally become aware of their prices only when there was co-operation on advertising. As retail margins were not high, there seemed unlikely to be significant changes in retail pricing policies if RRPs were abolished.

Consumer choice of outlets

7.6. Klein considered that selective distribution resulted in a very competitive retail environment. It encouraged retailers to compete in providing high-quality service and a wide choice of fragrances as well as a fair price.

Duty-free outlets

7.7. Klein said that it strove to ensure that its products were sold only through authorized duty-free and tax-free outlets satisfying its criteria. Sales through these outlets had the cachet associated with international travel and did not undermine the justification for selective distribution. Moreover, Klein had been advised by EC Commission officials that the Commission viewed the duty-free market as distinct from the domestic market. Klein considered that the criteria applied to duty-free outlets should reflect the particular circumstances of that market.

Discrimination against retailers

7.8. Klein considered its criteria for assessing outlets for authorization to be fair and to reflect the quality image associated with its products. The criteria were based on those in the EC Decisions and were applied in the spirit of the Decisions. Retailers who did not meet the criteria were notified of the reasons. If they could meet the criteria after making alterations they were given an opportunity to do so within a specified period.

7.9. Klein said that it was evaluating Superdrug outlets in response to that company's application. If they met the qualitative criteria, Klein's attitude to Superdrug would depend more on its approach to partnership in marketing the Klein brands than on the image projected by the Superdrug name.

7.10. Klein did not believe that a system of independent arbitration would be appropriate to deal with disputes over refusal to authorize outlets. It would add a layer of bureaucracy and the added expense could lead to higher prices.

The grey market

7.11. Klein said that grey markets existed in many products, whether or not they were subject to selective distribution. Traders would exploit price differences due to currency fluctuations or other causes. The grey market was to the detriment of consumers as the trade often involved discontinued, damaged, defective or out-of-date goods. Most grey-market supplies came from abroad and Klein took extensive measures to maintain product security in all the countries where its products were sold.

Counterfeit and replica fragrances

7.12. Klein was concerned about the extent of counterfeiting and said that the damage to its brands was increased by the appearance of counterfeits among genuine products in unauthorized outlets. Klein had been active in pursuing this problem and also in taking action against replica fragrances that breached its copyright.

Superdrug advertising

7.13. Klein said that it had not contacted any publisher of high-quality fashion magazines with a view to discouraging it from accepting Superdrug advertising for fine fragrances. Klein considered that publishers should be free to accept or reject advertising in the light of their own standards; conversely, advertisers should be free to cease advertising in publications which they regarded as no longer having the right image or readership.

Chanel Limited

Selective distribution

7.14. Chanel said that coherent brand strategies were essential to effective marketing and the conditions under which products were retailed formed part of those strategies. It emphasized that Chanel had an international brand image of luxury, quality, prestige and exclusivity which had been carefully developed and sustained over 70 years, embracing not only fragrance but also fashion (*haute couture* and ready-to-wear), accessories (including watches and jewellery), skincare and cosmetics. Retailing of Chanel fragrances through outlets which detracted from these perceived qualities would undermine the established image, not only of Chanel fragrance, but of the House of Chanel and its products generally. Selective distribution was essential to ensure that the perceived quality of Chanel brands was communicated and maintained at the point of sale. It provided key benefits to consumers by ensuring the availability of an adequate range of products in prime condition and maintaining standards of service (see also paragraph 3.69(a) to (e)).

7.15. Chanel pointed out that the significance of retail conditions to a supplier's individual brand strategy extended some way down the market. Thus Bourjois, Chanel's sister company, marketed cosmetics and a relatively inexpensive fragrance (which was, nonetheless, a reference product) without a policy of selective distribution, but would refuse distribution to market stall holders as this form of retailing would be incompatible with its image.

Shop name

7.16. Chanel emphasized the importance of the requirement that the retailer's trading name, style and reputation (the 'shop sign' or '*enseigne*') be compatible with the brand image and exclusivity attaching to the Chanel name. This requirement had been endorsed by the EC Commission in its Decisions on the YSL and Givenchy selective distribution systems. A survey commissioned by Chanel from Inform Research International had indicated that public perception of the 'shop signs' of Superdrug and Tesco was that they were likely to lessen the perceived image of Chanel brands. The incompatibility of the image of each of these companies with the Chanel image was a basic reason why Chanel had declined to authorize them, although in the case of Tesco there were also serious problems over the outlets themselves.

Retailers' costs

7.17. Chanel believed that the costs incurred by its authorized retailers were necessary to the realization of the image of Chanel as a luxury brand and were no more than the costs that Chanel would choose to incur if for any reason it were to go over to retailing its fine fragrances. It contributed substantially to their costs in respect of point-of-sale material and beauty consultants. Reduction in costs could not be equated *per se* with an increase in efficiency. The selective system provided an incentive to retailers to improve the effectiveness of retailing of Chanel products.

Stockholding requirements

7.18. Chanel said that its stockholding requirements were reasonable and had not given rise to any complaint from authorized retailers. Of the total number of lines, they were only required to hold two-thirds, in order to enable consumers to find the sort of choice they expected from Chanel authorized retailers. Retailers could return goods, subject to a handling charge of 25 per cent. Chanel saw no case for loosening the requirements, given that they were an important part of brand promotion and were pro-competitive in improving the availability of products to consumers.

Level of prices to consumers

7.19. Chanel pointed out that over the last decade sales of fine fragrances had risen in relation to sales of mass fragrances. This indicated that consumers regarded fine fragrance brands as being worth at least as much as the price premium associated with them at the point of sale. The market for fine fragrances showed vigorous competition at supplier level, with shifting fortunes of individual brands, houses and supplier groups. If margins were too high, competition would lead to reductions. Retail margins did not appear high in relation to margins on other products, allowing for the associated retailing costs of different products.

Recommended resale prices

7.20. Chanel said that recommending retail prices was not fundamental to its marketing strategy, but it was considered helpful to retailers to have an indication of a satisfactory retail margin in the context of fine fragrance retailing conditions. In its experience, retailers generally expected and welcomed such a service. If RRPs were prohibited, Chanel thought that some retailers might choose to increase prices slightly, increasing their margins to perhaps 40 or 41 per cent.

7.21. Chanel said that it did not withhold authorization from retailers on the grounds that they were likely to sell its products at less than the RRPs. Its authorized retailer agreement stated that retailers were free to determine the retail selling price of Chanel products sold by them. It had not withheld supplies from, or discriminated in any way against, a retailer on the ground of price cutting; this was prohibited under the Resale Prices Act 1976 and Article 85(1) of the Rome Treaty.

Consumer choice of outlets

7.22. Chanel said that selective distribution did not reduce consumer choice by preventing sale of its products through outlets offering lower prices, possibly with a lower level of service and ambience. There was nothing in selective distribution as practised by Chanel to prevent authorized retailers from offering lower prices, but if the high quality of point-of-sale conditions was not maintained, the brand would lose its place in the market. This had happened to Chanel in the USA and it had required substantial effort over a long period to regain market share. If some retailers were allowed to operate to lower standards of presentation and service, they would in effect 'free ride' on the investment in brand promotion by normal authorized stockists as well as their pre-sales advice. Consumers had a choice of outlets and of products within stores.

Duty-free outlets

7.23. Chanel said that the standards of retailing in duty-free outlets at UK airports were normally equal to those of any high street retailer. Operators of outlets on board ships were well aware of the need to provide added value in the form of high levels of service and luxury. Operational restrictions on board aircraft were well understood and accepted by travellers. Sales on board aircraft were felt to enhance, rather than detract from, the Chanel image.

Discrimination against retailers

7.24. Chanel said it was axiomatic that selective distribution involved differentiating between outlets; the important thing was that there should be equal treatment of equal situations. The only discrimination Chanel exercised in deciding whether to admit retailers to the selective distribution system was in differentiating between those outlets which met the objective selection criteria and those which did not. These criteria were applied even-handedly in respect of all categories of retail outlets. There was a large number of fine fragrance suppliers following different distribution policies and the market would determine the appropriateness or otherwise of the different criteria applied.

7.25. When retailers were rejected, Chanel's practice was to give reasons in writing. This enabled the retailer to make representations if the decision was based on incorrect facts or otherwise considered wrong; it also enabled the retailer better to understand what could be done to satisfy Chanel's requirements. Chanel did not believe that there was scope for an independent arbitrator to resolve disputes about authorization. These should be subject to the existing remedies: through the OFT, through the EC Commission, or through the courts in an action for damages. It pointed out that retailers were likely to have at their disposal the services of a trade association which could provide legal advice, adding that it had sought to maintain a regular dialogue with such associations on developments in the distribution of fine fragrances.

The grey market

7.26. Chanel acknowledged that a grey market was a potential consequence of any selective distribution system, without which there would be no distinction between authorized and unauthorized outlets. It considered that the grey market detracted from the benefits of the selective distribution system and therefore operated to the detriment of consumers. Chanel had taken strong measures to prevent leakage of its products to the grey market and had withdrawn supplies from authorized stockists found to have been involved in this trade.

Counterfeit and replica fragrances

7.27. Chanel was concerned to prevent counterfeiting of its products. It was also concerned about the marketing of replica fragrances and had brought a successful action for infringement of its trade marks.

Superdrug advertising

7.28. Chanel said that it had never sought to discourage any publisher from accepting advertisements from Superdrug or any other unauthorized retailer of fine fragrances. However, it did not encourage its authorized retailers to advertise Chanel fragrances in newspapers or magazines as it was concerned to ensure consistency of presentation of the Chanel image. In selecting media for advertising, it would only take account of advertisements from unauthorized retailers in a magazine if they were symptomatic of, or accompanied by, a decline in the magazine's image.

Parfums Christian Dior (UK) Ltd

Complex monopoly

7.29. Dior submitted that a complex monopoly situation should not be held to exist because of the practices of selective distribution and recommending resale prices. Both the EC Commission and the European Court of Justice (ECJ) held that such practices did not 'prevent, restrict or distort competition' under Article 85(1) of the EC Treaty, and accordingly the MMC should not do so for the purposes of section 6(2) of the Fair Trading Act 1973.

7.30. Dior argued that the practice of only supplying certain outlets was the very essence of a selective distribution system and the EC Commission had recognized that such systems could have pro-competitive, efficiency-creating effects. Several ECJ cases supported the view that the concept of selective distribution and the basic features of selective distribution agreements did not restrict competition under Article 85(1). Particular features of a selective distribution system, or its operation, might take it into Article 85(1) and the issue would then be whether exemption could be granted under Article 85(3). This was, however, a separate issue from whether Article 85(1) applied in the first place. Dior submitted that the correct approach would be for the MMC to determine the complex monopoly ground or grounds by reference to terms of agreements and practices which fell within Article 85, setting aside those terms and practices which did not fall within the Article.

7.31. Dior also argued that there was no authority in EC law for maintaining that the practice of recommending resale prices was contrary to Article 85(1) provided that it did not result in concerted practices at the retail level, or between retailers and suppliers. Dior referred to previous MMC reports in which the subject of RRP had been considered. In one of the cases (Matches and disposable lighters¹) the MMC had not seen the recommending of resale prices as giving rise to concern. In another (Ice Cream and Water Ices²) the MMC had found that the practice of some suppliers of recommending resale prices restricted competition and was one of three practices which formed the basis of a complex monopoly situation. The MMC had concluded in that inquiry, however, that the practice of recommending resale prices in the supply of reference goods did not operate against the public interest.

Selective distribution

7.32. Dior said that selective distribution was the only method of distribution capable of ensuring that the prestige and quality of the Dior house name and brands were maintained, which in turn was a condition of its products' success. This was to the benefit of retailers and consumers as well as fine fragrance houses. Experience had shown that a change of distribution policy by a reputable fine fragrance supplier could have a disastrous effect on sales. Parfums Coty was often cited as an example of a highly reputable fine fragrance house which had to close as a result of its decision to opt for mass distribution.

¹The supply of matches and disposable lighters: a report on the supply for retail sale in the United Kingdom of matches and disposable lighters, Cmnd 1854, March 1992.

²Ice Cream and Water Ices: a report on the supply in the United Kingdom of ice cream and water ices, Cmnd 7632, August 1979.

Shop name

7.33. In assessing the acceptability for authorization to sell Dior fragrances of well-known retailers such as Superdrug and Tesco, the trade name and reputation or 'shop sign' of the retailer was an important factor. Dior had undertaken a qualitative group interview survey which indicated that consumers associated Superdrug with a down-market image, would not want to see Dior products sold at Superdrug stores and thought that if they were, the Dior name would lose its exclusivity. This had played a part in Dior's refusal of Superdrug's application, although the Superdrug outlets covered by the application had all failed to meet Dior's qualitative standards. The principal areas of failure were the facade, window decoration, internal decor and overall appearance.

Retailers' costs and stockholding requirements

7.34. Dior pointed out that the EC Commission, in the YSL and Givenchy Decisions, had said that the reason for requiring retailers to make a minimum annual purchase of fragrances was to ensure that the supplier's costs were covered by an adequate volume of business and that the retailer contributed actively to enhancing the brand. Dior set the minimum quantity for each retailer by reference to average purchases for accounts of the same type in order to ensure fairness. For larger stores the minimum was just over £2,000 and for chemists a little less. The stockholding requirement was seen by the EC Commission as ensuring that customers could always find, at each outlet, the main products in each brand range. Dior had reduced the number of its fine fragrance SKUs from 143 to 89 between 1988 and 1993 in order to focus on faster-selling lines. Most Dior retail accounts ordered more than the minimum stockholding and purchase requirements. Dior did not consider that the requirements put undue pressure on smaller retailers.

Level of prices to consumers

7.35. Dior considered that manufacturing, wholesale and retail margins were not high on fine fragrances, taking account of the particular characteristics of the fine fragrance market, which required continuous innovation, promotion and advertising efforts. Substantial sums were incurred by manufacturers on the launch of new fragrances, for research and development, production, advertising and promotion. Wholesalers and retailers also incurred substantial costs on promotion, advertising, point-of-sale material and beauty consultants.

Recommended resale prices

7.36. Dior said that RRP's were the custom within the fine fragrance industry. They were requested by retailers, especially smaller retailers, as a starting point to determine their margin. Dior had considered whether to stop recommending retail prices, but the majority of its retailers wanted it to continue. It had always made it clear to its retailers, and had done so again at the time its new authorized retailer agreement was introduced, that retail prices were a matter to be determined by them.

Consumer choice of outlets

7.37. Dior pointed out that its products were available in more than 1,000 outlets throughout the UK, well distributed in all major urban areas, giving consumers good access to its products. Furthermore, there was fierce inter-brand competition. It did not consider that there was the possibility of choice between outlets offering high standards of presentation and service and others offering lower prices with a lower level of presentation and service, as the latter would undermine the prestige image of the fine fragrance houses, with damaging effects on sales (see paragraph 7.32).

Duty-free outlets

7.38. Dior considered that the duty-free market should be seen as a distinct channel of supply, but that the level of service and ambience was good in duty-free shops in airports and ships. Sales on board aircraft could be seen as an extension of ground services, though necessarily constrained by space limitations. The purchase of fine fragrances in duty-free outlets was associated with the 'glamour' of travel.

Discrimination against retailers

7.39. Dior had introduced a new authorized retailer agreement in the light of the YSL and Givenchy Decisions, to ensure in particular an objective and even-handed application of its qualitative selection criteria. To this end, there were different evaluation reports for chemists and for department stores to take account of their different circumstances. Management procedures, including random checks, had been introduced to ensure consistency in the application of the selection criteria. Before an outlet was evaluated, the criteria were made known to the retailer, who was also informed in writing subsequently of any elements which failed to meet the criteria and, if the applicant came close to satisfying them, of the improvements needed to obtain approval. This procedure was being followed in the case of existing outlets which had been re-evaluated against the new criteria, about one-third of which fell below the standards, some very marginally. In Superdrug's case, the outlets did not come close to satisfying the criteria and so under Dior's conditions of sale the discussion of improvements was not appropriate.

7.40. Against this background, Dior did not consider that independent arbitration was necessary. Any dispute which could not be resolved amicably could be brought before the courts. Dior pointed out that the EC Commission had encouraged national courts to deal with disputes regarding compliance with Articles 85 and 86 of the Treaty.

The grey market

7.41. Dior acknowledged that selective distribution could be said to encourage the grey market. To the extent that consumers were able to obtain fine fragrances at lower prices, the grey market could appear to be to their short-term benefit. However, it was detrimental to the consumer in that:

- products might be in poor condition due to age or stocking in unsuitable conditions, or counterfeit; and
- there was a limited range of products, with no assurance of continuity of supply, and a diminished level of service.

7.42. Dior took action to discover the sources of its products on the grey market. Some authorized suppliers found to be supplying the grey market had been taken to court (principally in France) and/or their authorization had been withdrawn.

Superdrug advertising

7.43. Dior said that it had not contacted any publisher to discourage the acceptance of advertising from Superdrug or any other unauthorized retailer of fine fragrances. Its approach to advertising in magazines where Superdrug advertisements appeared would depend on the impact of the advertisements on the image of the magazine.

Elizabeth Arden Limited

Selective distribution

7.44. Arden said that it was in the process of building up its brands in the market. To maximize its sales it was necessary to work through a selective distribution network, in order to ensure the availability of its products in retail outlets which were complementary to its brand image and quality, and to provide those retailers with marketing support.

Shop name

7.45. Arden said that in considering applications for authorization the name of a retailer would be considered in the context of the retail environment, both inside the store and in the surrounding area. If the ambience of the store and the surroundings were adequate, the name alone was unlikely to be a cause of refusal. Arden was in the process of evaluating Superdrug outlets, but would not refuse them authorization solely on account of the Superdrug name.

Retailers' costs

7.46. Arden did not consider that selective distribution resulted in unnecessary costs to the retailer or in a lessening of competition. Arden contributed to the costs of beauty consultants and point-of-sale fittings in some of its authorized outlets.

Stockholding requirements

7.47. Arden said that it had reduced the inventory of its brands to 90 units, or SKUs. No brand had more than 6 SKUs. It was very flexible in setting stockholding requirements for its retailers; it was not in Arden's interests to have large slow-turning inventories. Consumer demand was its guidance for stockholding.

Level of prices to consumers

7.48. Arden said that prices to consumers had to be considered against the very high costs of bringing a new fragrance to the market and then keeping it suitably positioned.

Recommended resale prices

7.49. Arden said that RRP's were traditional in the fragrance industry. They were a useful bench-mark for wholesalers, retailers and consumers. However, retailers determined the actual resale prices and Arden did not look to enforce its recommendations. If RRP's were abolished, some of the smaller retailers might need some help over the levels at which to set their prices.

Consumer choice of outlets

7.50. Arden said that the selective distribution system ensured a wide availability of fine fragrances in retail conditions which sustained their luxury image. It did not consider that the fine fragrance market could exist without this arrangement.

Duty-free outlets

7.51. Arden said that it sought to improve the ambience of its duty-free outlets where this was practicable. It did not consider that sales through these outlets invalidated the justification for selective distribution.

Discrimination against retailers

7.52. Arden said that it used objective criteria when evaluating a prospective retail outlet and these criteria were published with its retailer agreement, a revised version of which was under discussion with its authorized retailers. It expected all retailers to sign the agreement.

7.53. Although supermarket chains such as Tesco had new superstores which were much more up-market in style, Arden still saw difficulties over associating the sale of fine fragrances with self-service retailing of groceries.

The grey market

7.54. Arden did not believe that selective distribution in itself encouraged the existence of a grey market. Arden's brands had not figured largely in the grey market, but its existence appeared largely due to differences in the prices of the same products in different countries, whether caused by currency fluctuations or other factors. While consumers might see the availability of fine fragrances at lower prices as beneficial, there was a risk of being supplied with counterfeit, stale or damaged goods.

Superdrug advertising

7.55. Arden said that it had not sought to discourage publishers of high-quality fashion magazines from accepting advertisements from retailers offering cut-price fragrances. However, suppliers had to consider whether changes to the content of a publication reduced its value as a medium for advertising their products.

Estée Lauder Cosmetics Ltd

Selective distribution

7.56. Lauder told us that it operated selective distribution in order to ensure that its products were delivered to consumers through retailers providing the level of service and presentation appropriate to the quality, reputation and image of its brands. This applied not only to its fine fragrances, but to all its ranges of fragranced products and non-fragranced beauty and skincare products. The group was first and foremost a supplier of cosmetics, make-up and treatments, and of fragrances to a lesser degree, rather than a 'fragrance house'.

7.57. Lauder believed that selective distribution operated to the benefit of consumers, providing diversity of choice and levels of presentation and service which helped in making the choice, also reinforcing the exclusivity of brands which was an intrinsic part of their appeal to the consumer. Without selective distribution, the incentive to existing retailers to maintain standards of presentation and service would be undermined by other traders taking advantage of their marketing efforts to offer products at lower prices without making a comparable investment. This in turn could undermine the reputation of brand names. The skill, dedication and investment involved in creating and maintaining luxury brands was matched by the ease with which a brand could be destroyed through unsuitable retailing.

Shop name

7.58. Lauder said that it had obtained evidence from a reputable market research company as to whether the public images of Superdrug and Tesco were consonant with the public image of Lauder and its products. The evidence had been that they were not and that consumer perceptions of these companies' stores were substantially different from those of core Lauder outlets. These companies therefore fell short of the requirement permitted by the two EC Decisions that the shop name should reflect the prestige of the supplier's brand and should not be associated with any restriction in customer service or with a lack of attention to decoration.

Retailers' costs

7.59. Lauder considered that the requirements placed on authorized retailers were not unreasonable and were designed to ensure a high level of product presentation and customer service. Suppliers competed for the best locations in retail outlets and there was a constant exchange of information with retailers on matters affecting presentation and service. There was intense competition between suppliers and between retailers.

Stockholding requirements

7.60. Lauder said that it did not impose quantified minimum stock levels on its authorized retailers; rather they were required to stock a representative range of lines of the brands they sold, the precise mix being discussed with each retailer. Retailers were required to stock cosmetics and skincare brands as well as fine fragrance brands. Lauder recommended turning stock over four times a year to ensure freshness and operated a generous policy on returned goods which supported this aim, ensured that retailers were not left with slow-moving stock and helped to minimize retailers' costs.

Level of prices to consumers

7.61. Lauder said that the prices of fine fragrances reflected the high costs of developing, producing, launching, marketing and retailing these luxury products. It had been estimated that, industry-wide, only one in five new fine fragrances showed a recovery of the initial investment. Manufacturing, wholesale and retail margins were not high in relation to these costs. Retail margins were lower than those obtained by stores on many other products.

Recommended resale prices

7.62. Lauder said that it recommended resale prices to assist its authorized retailers, for the information of consumers, and to assist in positioning products in the market. Setting prices involved considerations of cost, volume expectations, the target consumer, the level of prestige and the price points of competitive products. Lauder would not be placed in an insurmountable difficulty if RRP's were abolished, but it saw no justification for this action, which would deprive retailers and consumers of valuable information. It did not seek to limit retailers' freedom to set their own prices and, while it did not systematically monitor their pricing policies, knew that its products were frequently sold below the RRP's.

Consumer choice of outlets

7.63. Lauder said that consumers could choose between a wide range of fine fragrances and other fragrances offered by different manufacturers and between a wide range of retail outlets. Competition at the retail level was vigorous. Distribution of fine fragrances through outlets offering lower prices, possibly with a lower level of service and ambience, would involve the lower-quality outlets free-riding on the efforts and expenditure of the high-quality retailers, who would in these circumstances be likely to stop their efforts to support the brands. The result ultimately would be to undermine the prestige of the brands and thus to deny the consumer the choice of such prestige brands.

Duty-free outlets

7.64. Lauder said that selling through duty-free outlets did not invalidate the justification for selective distribution. Outlets at airports were generally of a high standard and normally had trained beauty consultants in attendance. It was impossible to have specialized sales fittings on aircraft and ships, and while sales in these circumstances to some extent free-rode on the contribution of authorized retailers to brand image, the duty-free outlets were themselves contributing to that image. Duty-free shopping was a special experience associated with travel, which (particularly flying) was seen as a prestige activity.

Discrimination against retailers

7.65. Lauder said that applications for authorized status could be refused only on grounds covered in its new questionnaire/check-list for evaluating retailers, which was designed to avoid the possibility of discriminating unfairly against certain types of retail outlet (for example, retailers in out-of-town locations which could not be judged by the quality of nearby shops and outlets with no windows, though outlets with window

displays scored more highly). The effect was to measure objectively the overall quality and public image of a retail outlet without regard to the type of outlet as such. However, the public image of a supermarket chain like Tesco, with a good reputation as a food retailer, was not that of a place where people would expect to buy fine fragrances.

7.66. Lauder said that the criticism of delay in dealing with Superdrug and Tesco applications was unfair as Lauder, and probably all other fragrance houses, had been involved during 1992 in an intensive appraisal of their selective distribution procedures and the preparation of new documents for use throughout Europe as a result of the EC Decisions. As soon as the new procedures were ready in January 1993, Lauder had inspected the Superdrug and Tesco stores for which application had been made. Lauder then wrote to Superdrug and Tesco asking them to supply the requisite information concerning their stores; Tesco had not responded. The Verdict report confirmed the relatively low quality of Tesco's stores.

7.67. In the case of disputes between suppliers and retailers, Lauder considered that there were remedies available to an aggrieved retailer. A complaint could be made to the EC Commission if a retailer believed that a supplier was not complying with the terms of the EC Decisions on selective distribution. This involved relatively little cost to the retailer. A retailer could also seek an injunction through the county court or the High Court to restrain an alleged breach of competition law, or damages, although this was more costly. Lauder did not consider that there was any justification for introducing a system of independent arbitration to resolve disputes because this could lead to a proliferation of vexatious claims and increased costs for the industry.

The grey market

7.68. Lauder acknowledged that the existence of a grey market was dependent on the existence of selective distribution, which distinguished between authorized and other retailers. The grey market constituted unfair competition in that unauthorized retailers could use a lower cost base to undercut authorized retailers, while free-riding on their expenditure and efforts. It was to the detriment of consumers in that it could undermine the standards of service and presentation available. It also provided no certainty of supply or of the quality or freshness of the products on offer.

7.69. Lauder said that goods were diverted to the grey market from a variety of sources, including authorized suppliers in overseas markets where supplies were higher than the true demand. It was taking active measures, on an international basis, to trace sources of grey-market supplies and stop them. Authorized traders found to be diverting supplies outside the authorized network had their authorization withdrawn.

7.70. Lauder was also concerned about grey-market sales of its products through unauthorized outlets of retailers who had other branches which were authorized Lauder outlets. In this context Lauder had negotiated a special arrangement with Lloyds Chemists, when it acquired a company with outlets authorized by Lauder, under which customers of a limited number of unauthorized Lloyds branches, in towns with no authorized source of Lauder products, could order from a restricted range of Lauder products and have them sent by an authorized branch, to be collected by the customer from their local unauthorized branch. No Lauder goods were stocked at the unauthorized location. In return, Lloyds had undertaken to cease trading in grey-market Lauder products. Lauder stressed that this was a unique and temporary arrangement, in order to make inroads into the grey market, which had involved a very small quantity of merchandise and was not inconsistent with its selective distribution policies.

Replica fragrances

7.71. Lauder was concerned about the marketing of replica fragrances, particularly when advertised as alternatives to particular Lauder fragrances, and had taken action under copyright law where appropriate. The presence of replica fragrances in outlets in respect of which approval was sought would be a factor in assessing their suitability.

Superdrug advertising

7.72. Lauder said that it had not put any pressure, either directly or through a trade association, on newspapers or magazines to refuse Superdrug's advertisements. While it did not welcome advertisements for grey-market products, it would not cease advertising in the publications it regularly used because they published such advertisements.

Giorgio Beverly Hills Incorporated

Complex monopoly

7.73. Avon Cosmetics Ltd, an affiliate of the same group as Giorgio, argued that, although it manufactured fine fragrances for Giorgio using materials which Giorgio provided, this was entirely an arm's length relationship and Avon was in competition with third party manufacturers for the business. Giorgio confirmed this.

Selective distribution

7.74. Giorgio said that selective distribution was essential to ensure that its products were sold through outlets with a level of service and facilities compatible with their up-market brand image, with staff having the appropriate technical expertise and experience. This was in the consumer's interests. There had been many instances of premium fragrances going down-market for short-term gain and losing sales and profitability.

Stockholding requirements

7.75. Giorgio said that consumers wanted a full product range, available on demand. The minimum stockholding requirement for authorized retailers was quite reasonable at a retail value of £3,500, one-third of the minimum annual turnover.

Level of prices to consumers

7.76. Giorgio said that there was intense competition among fine fragrance suppliers, with an increasing number of new products. Margins for manufacturers, wholesalers and authorized retailers and prices to consumers were not high in relation to costs.

Recommended resale prices

7.77. Giorgio said that pricing was an integral part of market strategy for fine fragrances. Recommending retail prices encouraged an orderly market. Abolition would lead to consumer confusion about the relative value of products.

Consumer choice of outlets

7.78. Giorgio said that the spread of authorized outlets provided full choice for consumers of fine fragrances, who expected a high level of service and an up-market ambience.

Duty-free outlets

7.79. Giorgio considered that air and sea travel was seen as a prestigious activity. Duty-free shops at major airports and on the newer sea ferries had been raised to a high standard of ambience. There were obvious

space limitations on aircraft. Sales in duty-free outlets did not invalidate the arguments for selective distribution.

Discrimination against retailers

7.80. Giorgio said that it had applied the criteria for assessing outlets for authorization regularly and consistently. The pricing policies of retailers were not taken into account. It had told Superdrug that it was not opening any new accounts until the MMC inquiry was finished, but that outlets which met the criteria would be supplied. It had not received an application from Tesco. In the case of a dispute between a supplier and a retailer, the remedy lay through the courts and it saw no requirement for an independent system of arbitration.

The grey market

7.81. Giorgio did not consider that the selective distribution system contributed to the existence of the grey market. Such fringe markets took advantage of exchange rate movements, oversupply in some areas, disruption to markets caused by wars and disturbances, counterfeiting and theft. Giorgio took extensive measures to prevent its products getting into the grey market. It had also had to take active measures against counterfeiting.

Superdrug advertising

7.82. Giorgio said that it had not discussed the question of Superdrug advertisements with any publishers of high-quality magazines. It would continue to use advertising media which reached its target market.

Parfums Givenchy Limited

Selective distribution

7.83. Givenchy said that an integral part of the image sought by many fine fragrance consumers when choosing a brand was an aura of exclusivity. The elements involved in creating and maintaining a fine fragrance brand included the public image of both supplier and retailer; presentation at the point of sale; and the support available to purchasers. It was necessary to restrict distribution to retail outlets which contributed to these elements by offering a wide range of fine fragrances and complementary products in attractive surroundings and employing trained staff able to offer advice on the products. Some fine fragrance suppliers who had abandoned selective distribution had lost the exclusive image, and wider distribution had resulted in reduced sales.

Shop name

7.84. Givenchy drew attention to the condition set out in its EC Commission Decision that a shop name must not, in the public's mind, be associated with any restriction in decoration or service. It said that there was a problem at the present time with the image projected by the Superdrug name, not because of its pricing policy, but because Superdrug's approach hitherto had been to concentrate on basic, everyday commodities. This image might well change over time and Givenchy expected to keep the position under review. Superdrug had requested assessment by Givenchy of only one of its stores and that was found not to meet the approved criteria. Tesco had not applied to Givenchy to be an authorized retailer, but a similar image problem might be expected to arise if it did.

Retailers' costs

7.85. Givenchy said that selective distribution did not lead to any significant increase in retailers' costs. The requirements placed on retailers under the selective distribution system were to a considerable extent standards which the retailers would wish to meet in order to satisfy their customers. Givenchy sometimes contributed to the cost of beauty consultants and provided point-of-sale material free of charge.

Stockholding requirements

7.86. Givenchy said that stockholding obligations were an inherent feature of selective distribution, as had been recognized by the EC Commission in its Decisions. It was in the collective interest of retailers that a full range of products was available to consumers, even though they might individually like to stock only the best-selling lines. Givenchy did not believe that it placed an unreasonable burden on retailers by requiring them to hold two-thirds of the total number of lines and make minimum annual purchases of £[*] (fine fragrances only) or £[*] (fragrances and cosmetics), at trade prices.

Level of prices to consumers

7.87. Givenchy pointed out that there was a large number of suppliers to the fine fragrance market and vigorous inter-brand competition. While consumers expected to pay more for a luxury product, a fragrance which was seen as too expensive would not sell. Retail margins were not high in relation to those for other products and manufacturers' and wholesalers' margins were not high, taking account of the costs they incurred.

Recommended resale prices

7.88. Givenchy said that it had been regarded as helpful to retailers to notify RRPs, which also made it easier for consumers to compare prices. Although the supply agreement between Givenchy and its parent company Parfums Givenchy SA required Givenchy to devote all its efforts, within the laws of the country, to cause retailers to apply RRPs, this was null and void in the EC. Any attempt to encourage retailers to adhere to RRPs would be a breach of the terms of the EC Decisions and, in Givenchy's case, of an undertaking it had given to the DGFT in 1989. Givenchy acknowledged that the presence of this provision was anomalous. In France, Parfums Givenchy SA had abandoned the practice of notifying RRPs at the request of the national competition authority.

Consumer choice of outlets

7.89. Givenchy said that if fine fragrances were freely available in any type of outlet their exclusivity would be destroyed and they would rapidly lose their attraction. There was, however, a range of choice among authorized outlets, from large department stores to small chemists.

Duty-free outlets

7.90. Givenchy considered that duty-free shops at major airports, which were of a high standard, could be said to enhance the brand image of a fine fragrance by associating its purchase with foreign travel. This consideration also applied to sales on ships and aircraft. Although space limitations made it impossible to provide the full range of products and service on aircraft, crew selling fragrances received similar training to staff of other authorized retailers.

*Figures omitted. See note on page iv.

Discrimination against retailers

7.91. Givenchy said that it applied the criteria for authorizing retail stockists on a non-discriminatory basis. Certain types of outlet would generally fail to achieve the aim of reinforcing the image of luxury and exclusivity and if so, had to be excluded. Givenchy's new authorized retailer system was still in the process of being introduced and it was possible that some existing outlets might not qualify.

7.92. If there was a dispute between a supplier and a retailer, it was open to the retailer to make a complaint to the EC Commission or to the UK competition authorities. Action could also be taken in the English courts. Although it was too early to judge whether the new selective system was likely to lead to such problems that some form of independent arbitration would be justified, Givenchy considered that it was unlikely to be needed and was concerned at the possible cost. No system of independent arbitration operated in other EC member states, where remedies were sought through the courts.

The grey market

7.93. Givenchy considered that selective distribution encouraged the existence of a grey market, which was relied on by retailers who were unable to obtain authorized supplies of fine fragrances. This presented a significant problem for Givenchy, not because unauthorized retailers sold at discounted prices, but because they sold a very limited range of products, often from unsuitable premises with unqualified staff, and therefore damaged the brand image. Givenchy tried very hard to prevent its products getting on to the grey market and had closed the accounts of authorized retailers and distributors found to be responsible.

Counterfeit and replica fragrances

7.94. Givenchy had taken action at an international level to combat counterfeiting. It was also concerned about the impact on the brand image of replica fragrances and had succeeded in getting the manufacturers to withdraw a cheap fragrance with a similar name and packaging to a Givenchy product.

Superdrug advertising

7.95. Givenchy said that it had made no attempt to discourage publishers of high-quality fashion magazines from accepting Superdrug advertisements, although it had been told by one publishing house that it had rejected such an advertisement. Its decisions on where to place its own advertising were not influenced by whether a publication had accepted advertising from unauthorized retailers of fine fragrances, but by the overall focus of the publication.

Guerlain Ltd

Selective distribution

7.96. Guerlain said that its major asset was its brand image of luxury and quality, which had been built up over 165 years. Its customers expected a high level of service and ambience. This meant that its products could not be sold in all retail environments. Selective distribution was necessary to ensure consistency between the luxury brand image and the retailer. This applied to prestige skincare and cosmetics as well as fine fragrances; all three were interrelated in terms of marketing strategy.

Retailers' costs

7.97. Guerlain acknowledged that its selective distribution system involved more costs for retailers than supplying some other products, but pointed out that such costs applied elsewhere in the luxury personal goods market. Consumers buying fine fragrances expected a high level of pre-sales service and ambience and were willing to pay a premium for that. Guerlain incurred substantial costs in respect of all its retailers, including display and tester materials, staff training and sales support.

Stockholding requirements

7.98. Guerlain said that it had certain minimum stockholding and range requirements in order to provide consumers with an adequate choice across its product range, but these only imposed a marginal financial burden on the retailer. The cost (at wholesale) of the average minimum opening order, and thereby the stockholding requirements for all Guerlain products, ranged from £7,500 for an average department store to £2,500 for a pharmacy or specialized perfumery. This was not unreasonable if customers were to be attracted and retained.

Level of prices to consumers

7.99. Guerlain said that it did not start from the premise of equating high prices with luxury. It did not consider that the retail prices of its fragrances were high in relation to the costs of producing and marketing them. Manufacturing and wholesale margins were not excessive in relation to the costs of research, development, production and marketing. Retail margins were consistent with a high-value product, of relatively low stockturn, and were lower than on other products such as fashion accessories and hosiery.

Recommended resale prices

7.100. Guerlain said that RRPs were of significant assistance to retailers as a guide to setting retail prices but were not fundamental to its strategy in the long term. Guerlain did not interfere with the margins which its retailers established, nor monitor retail prices. Its RRPs operated more as a *de facto* maximum than as a minimum price. Guerlain said that there had been cases where unauthorized retailers had quoted incorrect RRPs for its products when making discount price comparisons. The effect of abolishing RRPs was difficult to forecast, but it could lead to some increase in retail price levels.

Consumer choice of outlets

7.101. Guerlain said that selective distribution did not inhibit competition between retailers, nor did it create difficulties for consumers in obtaining products. Consumers had a wide range of choice of fine fragrance brands in shops offering a high level of service and ambience. There was also ample choice of less expensive fragrances marketed by other companies, which were sold more widely with a lower level of service and ambience. If some retailers within the selective system were able to offer fine fragrances at lower prices and levels of service, they would free-ride on the investment of others in the brand image of the product; this would undermine the high-quality outlets, leading eventually to the loss of such facilities to consumers.

Duty-free outlets

7.102. Guerlain said that many duty-free shops were fully in accord with its brand image. Conditions were different on board ships and aircraft, but duty-free sales in these surroundings were an adjunct to international travel, which was linked to a sophisticated lifestyle.

Discrimination against retailers

7.103. Guerlain said that it supplied department stores, retail pharmacies, perfumeries and beauty salons. Its criteria for authorization were applied consistently across all outlets world-wide and it did not discriminate in any way against retailers which did not conform to RRP. It did not supply drugstores (in the European sense of the term) or supermarkets as their marketing style and image were not compatible with the Guerlain brand image. It would not therefore supply Superdrug or Tesco.

7.104. Guerlain pointed out that, in the event of a dispute with a supplier, a retailer could complain to the OFT or to the EC Commission, either of which had powers to investigate the complaint and take appropriate action. The cost of pursuing these courses was very small. Remedies could also be sought through the courts for breach of the Resale Prices Act 1976, section 11, where a refusal was based on price discounting, or for breach of statutory duty under Article 85(1) of the EC Treaty. Where damages claimed were below the appropriate limit, action could be initiated at county court level. Guerlain did not consider that there was any justification for creating a system of independent arbitration.

The grey market

7.105. Guerlain acknowledged that the selective distribution system, by restricting supplies to authorized retailers, resulted in a demand for supplies outside the system. Unauthorized retailers with access to grey-market supplies could take a free ride. This was damaging to the system and potentially harmful to consumers as there was a likelihood of poor-quality stock and counterfeiting. Guerlain took every reasonable step to prevent its products getting into the grey market and authorized retailers found to be repeatedly responsible had their authorization withdrawn.

Counterfeit and replica fragrances

7.106. Guerlain was concerned that, while the volume of counterfeit goods was small, it was growing. Recent penalties on conviction were not strong enough to deter. Replica fragrances were also a problem and Guerlain had a current dispute with the manufacturer of such a fragrance.

Superdrug advertising

7.107. Guerlain said that it had not initiated any discussions with publishers about Superdrug advertising of fine fragrances in their magazines. The magazines it advertised in were chosen because of their consumer profile, blend of advertisers and attitude to beauty and healthcare.

Muelhens Ltd

Selective distribution

7.108. Muelhens said that, as a recent entrant to the UK market, it was essential for it to maintain a system of selective distribution, focusing on department stores and premium perfumeries, in order to build up the image and market share of its brands. On taking over the UK distribution of its brands it had found it necessary to dispense with a considerable number of retail outlets which had very low levels of sales. It had reduced the total number of outlets by three-quarters while increasing gross sales income to three times the previous level. This illustrated the need to sell premium fragrances through high-quality outlets. Consumers did not look to buy these products in down-market outlets, which detracted from the brand image.

Stockholding requirements

7.109. Muehlens said that quality retailing was about offering the consumer a breadth of choice of brands and a depth of choice of product types and sizes within brands. Poor retailers 'cherry-picked' fast-selling lines and this led to reduced consumer choice. Muehlens reviewed the stockholding requirements placed on its retailers in the light of sales levels. Retailers could return goods, normally getting credit for the full wholesale price.

Level of prices to consumers

7.110. Muehlens said that price was related to brand positioning in the market, which determined the quality and therefore the cost of many elements of the product and its packaging. Manufacturing, wholesale and retail margins were not high in relation to costs. Muehlens pointed out that very high costs were incurred by new entrants to the market and on the launch of new brands, and drew attention to a report in the *Financial Times* that only a fifth of fine fragrances launched now recoup their launch costs within three years, compared with a half six years ago.

7.111. Muehlens told us that it had pointed out to Superdrug that if discounting by Superdrug led to other retailers discounting, they might seek to restore their margins by forcing a cut in Muehlens' margin. This would force Muehlens out of business.

Recommended resale prices

7.112. Muehlens said that recommending resale prices positioned brands in the market. RRP's served as a yardstick to the retailer to indicate a reasonable retail margin and to the consumer to judge whether a product was a premium, mid- or mass-market brand. However, retailers were free to determine their retail prices and to compete with each other on price.

Consumer choice of outlets

7.113. Muehlens said that its objective was to make its brands available nation-wide, through high-quality outlets of the kind where consumers would expect to find them. The ambience of such outlets and the service and advice they provided were to the benefit of consumers. The variety of high-quality outlets selling Muehlens' brands, with their various retailing formats, added to consumer choice.

Duty-free outlets

7.114. Muehlens pointed to a number of examples where perfumeries at major international airports outclassed many domestic retail outlets. Conditions on board aircraft were different, but travel on world class airlines continued to have the image of luxury. Availability of Muehlens' products on such airlines did not detract from their image.

Discrimination against retailers

7.115. Muehlens pointed out that setting quality standards for entry to the selective distribution system involved discrimination and those not meeting the standards might perceive them to be unfair. Muehlens operated on very strict quality standards which were not met by many outlets currently authorized by some other suppliers. This reflected a need to ensure that Muehlens' brands were in outlets whose retailing conditions matched the expectations of its customers, and not a desire to limit numbers.

The grey market

7.116. Muelhens acknowledged that limiting the availability of goods and services encouraged the creation of a parallel market. In the short term the grey market for fine fragrances could operate to the benefit of consumers. However, grey-market retailers tended to carry only the best-selling lines of the top brands, riding on the back of the investment in the brand image. In the long term this could downgrade a valuable product to a commodity, perhaps leading to its disappearance from the market.

Replica fragrances

7.117. Muelhens said that the selling of replica fragrances, or designer alternatives, detracted from the standing of the fine fragrances whose image was being copied. This was particularly detrimental if the replicas were sold in the same stores as the original. For that reason, Muelhens would not supply any retailer which sold replicas, as Superdrug did at present, and it had so informed Superdrug.

Superdrug advertising

7.118. Muelhens said that it had not approached any publishers about acceptance of Superdrug advertising of fine fragrances in their magazines. Muelhens carefully selected the publications in which it advertised to enhance its brand names and would review this choice if a publication were to devalue its image by virtue of its content or the quality and style of the advertisements.

L'Oréal (UK) Ltd

Complex monopoly

7.119. L'Oréal told us that, of its three UK operating subsidiaries with interests in fine fragrance distribution, this was the core business of P&C, but not of Golden and Parim (Lancôme). P&C therefore acted as spokesman for all three companies. Accordingly, statements attributed to L'Oréal in this chapter apply to all three subsidiaries. Where statements apply to only one subsidiary, it is named. L'Oréal said that neither it nor any of its operating subsidiaries had any agreement with any of the other companies which the MMC provisionally identified as forming a complex monopoly in the fine fragrances market. It did not consider that the coupling of the practices of selective distribution and recommended resale prices justified that finding. It drew attention to a report by Lexecon Ltd (specialists in economic and regulatory affairs) which, it said, showed that the fine fragrance industry in the UK was highly competitive and that the major players did not and could not so co-ordinate their activities as to prevent, restrict or distort competition. The EC Commission had recognized not only the need for selective distribution but also that it enhanced competition.

Selective distribution

7.120. L'Oréal said that the experience of certain brands had shown the absolute necessity of presenting fine fragrances, as luxury products, in a consistent manner which conveyed the image of luxury to the consumer. Where suppliers had ceased to respect this fundamental rule, their brands had lost both their luxury image and their market share. If a fine fragrance brand image was to be preserved in the long term, each retailer selling it must meet the qualitative criteria appropriate to the market positioning and profile of the brand; otherwise, the investment which went into creating the fine fragrance would be wasted. Consumers had high expectations of fine fragrances and selective distribution protected their interest in quality, range of choice, service and advice.

Shop name

7.121. P&C said that the basic reason it had rejected Superdrug's application for authorized status was that its name carried the reputation of a down-market retailer of inexpensive products. The overall selling environment of Superdrug stores was designed to sell products with a very different image to luxury fine fragrances. Consumers did not instinctively think of Superdrug as an outlet in which to purchase luxury goods. P&C had a number of concerns about the stores themselves, including the level of decor and the range of products stocked. The name was also a problem with Tesco.

Retailers' costs

7.122. L'Oréal said that the conditions required of its authorized retailers were essential to the maintenance of an appropriate selective distribution system and did not cause any unnecessary increases in retailers' costs. The direct costs of becoming an authorized P&C retailer, in P&C's experience, rarely exceeded £7,000 and on average would probably not exceed £4,000. These costs were not at a level which could be said to limit entry to the market. There had been no weakening of competition at retail level. P&C had some 1,800 retail outlets and there was active competition between them.

Stockholding requirements

7.123. L'Oréal said that consumers expected to find a good choice of fine fragrance products in authorized outlets. Authorized P&C retailers had to hold two-thirds of the lines of each of the brands stocked and stock all the brands of each house (eg Cacharel) they decided to take. They also had to rotate the stock at least twice a year. Parim (Lancôme), which had a somewhat different product range, required a representative assortment of lines across the range to be stocked. While contracts with authorized retailers provided for them to make a minimum annual order, P&C did not currently set such a minimum. Stockholding costs were modest and any possible disadvantage to smaller retailers was mitigated by the practice of taking back products not required by the retailer at a cost-based handling charge of 15 per cent.

Level of prices to consumers

7.124. L'Oréal said that there was a wide range of prices for fine fragrances. Prices to consumers were not high. Retail margins were typically around 37.5 per cent, much lower than for other products such as suncare products. Wholesalers contributed to the costs of authorized retailers and had heavy advertising and promotional costs, particularly on newly-launched fragrances. The high cost of developing and launching a new brand meant that, while an established and successful fragrance like Loulou might provide a good net margin, some new fragrances produced negative net margins in the early years.

Recommended resale prices

7.125. L'Oréal said that RRPs were used because retailers asked for guidance on pricing. This was particularly important at the time of a product launch when retailers had little or no experience of the fragrance in question. Retailers were, however, free to ignore this advice. Selective distribution was not used as a means of maintaining resale prices. L'Oréal said that there had been cases where an unauthorized retailer had made an incorrect claim about the RRP of one of P&C's products in a discount price comparison.

7.126. With the evolution of the market, P&C had come to the view that RRPs had become more important to unauthorized retailers as a discount point than to authorized retailers, whose pricing freedom should be recognized. P&C had therefore recently decided to cease to include RRPs in its price lists and to rely instead on the trade prices and retailer experience supplemented by discussions with appropriate P&C personnel. Large retailers had appeared quite content with this decision and there had been few objections from smaller retailers, but some chemists had experienced difficulty. One large retailer had as a consequence slightly increased the price of some lines, while others had made some reductions. P&C had known that its initiative entailed certain risks and was monitoring the situation, but it was too early to assess consumer

reaction. It would probably give retailers a guide to the market positioning of new brands when they were launched. In France, where similar action had been taken, RRP's had been discontinued on some products in pharmacies at an earlier stage, at the request of the authorities.

Consumer choice of outlets

7.127. L'Oréal said that it would not be possible to maintain an appropriate network of retailers providing high quality and service in the face of competition from determined 'no-frills' retailers offering lower prices on a platform of lower service and selling environment. In the short run consumers might gain from lower prices, but in the long run the luxury presentation, service and advice would disappear.

Duty-free outlets

7.128. L'Oréal said that, although selective distribution was largely based on shops, the criteria used were not intended to prevent sales through other outlets, provided they met the objective of maintaining the luxury image. Airport duty-free shops were of a high standard. Where sales on ships and aircraft were concerned, international travel was still, for the majority of people, a luxury and duty-free retailing in this environment did not cheapen the image of fine fragrances.

Discrimination against retailers

7.129. L'Oréal said that the criteria for assessing retail outlets were applied in a uniform and non-discriminatory fashion to all categories of outlet. If a retailer was rejected, a full explanation of the reasons was given and a further application could be made when the problems were dealt with. Refusal to supply an outlet solely because of the possibility, actual or perceived, of discounted prices was contrary to EC law and a reference in the draft Lancôme check-list for assessing outlets to assessing a retailer's name partly according to whether it had any 'possible similarity with a name known for cut prices' as an adverse factor would be revised. The section in question was concerned with the name and reputation of a retail outlet and it was not intended to base a rejection on the cutting of prices as such. This form of check-list had not been used in the UK.

7.130. L'Oréal did not believe it was necessary to introduce an independent arbitrator to deal with disputes between retailers and suppliers about authorization. The most appropriate course for an aggrieved retailer would be to claim redress through the county court. The national courts had concurrent jurisdiction with the EC Commission in the enforcement of EC competition rules and, unlike the EC Commission, had power in appropriate cases to award damages and costs. The EC Commission might decline to accept a complaint in cases where the claim could be regarded as unimportant either in economic terms or in terms of legal precedent and redress was available at national level.

The grey market

7.131. L'Oréal acknowledged that any selective distribution system could be expected to encourage a grey market in as much as some retailers unable to meet the standards would want to sell the product. Variations in prices between countries caused by fluctuations in exchange rates, local costs and taxes provided an incentive to divert supplies from the authorized system. Consumers might benefit from lower prices in the short term, but in the long term grey-market activity could degrade fine fragrances and destroy the elements of luxury and choice which appealed to the consumer. L'Oréal took a variety of measures to identify sources of supply and stop authorized traders supplying the grey market. Failure to comply meant exclusion from the authorized system. Retailers selling grey-market fragrances who applied for authorization would not be accepted unless they agreed to stop doing so.

Superdrug advertising

7.132. L'Oréal said that its subsidiaries (P&C, Golden and Parim) had not approached any publishers about acceptance of Superdrug advertising of fine fragrances. As an advertiser, however, it had a legitimate concern about the style and content of magazines, including the advertising. If advertising were to appear which risked changing the image and reputation of the magazine or of L'Oréal's products, it would give its opinion, since it did not make commercial sense to advertise in a magazine which was not in harmony with its products. When Lancôme (Parim) became aware that *Hello!* magazine had published Superdrug advertisements for cut-price fragrances, it had told the publisher that there was no coherence between the advertisements of fragrance houses and those of discount stores whose main offering was everyday, household products. This juxtaposition could be expected to degrade the standing of the quality brands. Lancôme had advertised in *Hello!* since its launch and considered that it had a particular relationship with the readers. P&C, which also advertised in *Hello!*, had made no approach to the publisher.

Sanofi Beauté Ltd

Selective distribution

7.133. Sanofi regarded selective distribution as vital to the sale of fine fragrances in order to maintain and protect the element of luxury within them. Luxury comprised name, product quality and range, service and environment. Because the luxury image of the brands was transmitted at each point of sale, the marketing investment available had to be focused on outlets which were able to participate fully in the marketing programmes. Sanofi believed that allowing general distribution of its products would be uneconomic, since the additional administrative and marketing costs which this would involve would not be matched by a corresponding increase in sales, and distribution costs would become disproportionate to turnover.

Retailers' costs

7.134. Sanofi did not believe that retailers' costs were too high. Although requirements under the selective system increased retailers' costs, Sanofi believed that they were justifiable. They had been recognized in the EC Decisions as contributing to improved distribution of fine fragrances and benefiting the consumer. Advertising and promotional activities were in the interest of both supplier and retailer and were in any case funded almost exclusively by the supplier.

Stockholding requirements

7.135. Sanofi marketed fine fragrance products under four different house names and would conclude separate retailer agreements for each. Under these agreements retailers would be required to stock two-thirds of the references of each brand within a house name, with at least one unit of each such reference. This would enable the retailer to provide a comparable product if a particular item was unavailable, while stock rotation ensured that the products were fresh. These requirements were necessary to ensure consumer choice and were recognized as reasonable in the EC Decisions. Without the two-thirds stocking obligation Sanofi considered it unlikely that it would be able economically to continue to produce the entire range of references for a line.

7.136. Sanofi said that retailers had considerable scope within the stockholding requirements to choose the references which they thought would be most popular with consumers. Moreover, in recent years retailers had acquired greater bargaining power and if there was insufficient demand for a particular reference they were likely to discuss the problem with the supplier with a view to delisting or replacing it.

Level of prices to consumers

7.137. Sanofi did not believe that the prices of fine fragrances were too high. Rather they reflected the fact that they were luxury products, the creation of which required considerable investment by the supplier. The performance of luxury products was also very important to consumers, so they had to represent good value for money. If consumers regarded the prestige or brand image or the services and environment associated with the sale of the products as secondary to price they were free to choose non-luxury items distributed without the benefits of a selective distribution system.

Recommended resale prices

7.138. It was customary in the UK to advise an RRP which included the generally accepted retail margin for fine fragrances. Sanofi had recently suggested to retailers that this custom might be discontinued but had found that its customers, particularly the smaller ones, preferred to see the service maintained. To this extent the recommending of resale prices was customer driven but not essential. Sanofi did not believe that it restricted competition. Retailers were free to set their own resale prices and they were aware of this. Sanofi did not believe that suppliers' recommended prices had any effect on price competition among authorized retailers. However, there had been cases of unauthorized retailers making incorrect statements about the RRPs of Sanofi's products in discount price comparisons. Sanofi's experience in the French market had shown that the discontinuation of the practice of recommending resale prices had had little effect on relative retail price levels.

Consumer choice of outlets

7.139. Sanofi said that fine fragrances were sold in a large number of outlets and therefore it did not accept that consumer choice was restricted. Selective distribution enabled consumers to buy from retailers which provided choice, assistance, value and a quality environment. They were not forced to buy products which were distributed in this manner, and remained free to buy other fragrance items which competed with fine fragrances and which had a broader distribution.

Duty-free outlets

7.140. Sanofi considered that the service and ambience levels in duty-free shops and on board ships were in general comparable with those of authorized retailers. Sales on aircraft were a special case and in no way invalidated the justification for selective distribution.

Discrimination against retailers

7.141. Sanofi said that it sought to apply its qualitative criteria in a fair and non-discriminatory manner to all would-be authorized retailers. It would not object to selling through a drugstore if the shop name carried no unfavourable implications and if the service, ambience and general quality of the environment were right. Supermarkets presented more difficulties. Consumers did not currently seem to regard them as an appropriate place to find fine fragrances. However, Sanofi was aware of moves by supermarkets to create separate environments within individual stores which would be different and which could be evaluated according to Sanofi's criteria.

7.142. Sanofi believed that a system of independent arbitration to deal with disputes between suppliers and retailers about authorization would be costly (in which case it would be unlikely to be used) or would impose undue burdens on suppliers in dealing with disappointed retailers. Articles 85(1) and 86 of the EC Treaty created direct rights which were enforceable in national courts. In Sanofi's view aggrieved retailers had a satisfactory remedy available in the ability to sue in a national court. They could also make a complaint to the OFT or to the EC Commission, procedures that were simple and inexpensive. Sanofi pointed out that the EC Commission had fined AEG ECU 1 million for refusing to admit to its selective distribution network dealers who met the necessary qualitative criteria.

The grey market

7.143. Sanofi believed that the growth of the grey market was an unfortunate side-effect of the selective distribution system. Grey markets existed in other markets where selective distribution was practised (eg the pharmaceuticals and motor vehicle industries) and should therefore not be considered as unusual. The existence of unauthorized retailers was likely to contribute to a lower perception of the brands in which the supplier had invested and poor service levels for consumers. Sanofi understood that the grey market in France was smaller than in the UK and thought that one of the reasons for this was that suppliers were tougher in enforcing the selective distribution system there.

Counterfeit and replica fragrances

7.144. Sanofi said that in 1991 it had been advised by a Trading Standards Officer that counterfeit versions of its products were being sold and it had assisted him in tracing the source of the products. Although replicas of some of its products had also been produced this had not been a major problem for Sanofi.

Superdrug advertising

7.145. Sanofi said that it had had no contact with publishers to discourage them from accepting advertisements from Superdrug or from any other person or company, nor would it see any reason to do so.

Parfums Yves Saint Laurent Limited

Selective distribution

7.146. YSL said that the essential characteristics of fine fragrances were high quality, a prestige house or brand name and marketing and distribution in a manner consistent with the prestige of the brand and the quality of the product. YSL's fine fragrance products were part of the 'world' of Yves Saint Laurent, one of the greatest fashion designers of the 20th century. The EC Commission had recognized that distribution of a luxury cosmetics brand must be on an exclusive basis in order to enable the manufacturer to maintain an original and prestigious brand image. The way in which a fine fragrance could lose its aura and prestige if it was not properly marketed and distributed had been demonstrated by the experience of Coty in the 1920s and 1930s: because it had not followed the general move to specialist perfumeries as the main channel of fine fragrance distribution in France, the former high prestige of its name was undermined and it lost its place in the market.

Retailers' costs

7.147. YSL pointed out that all the requirements it imposed on its authorized retailers had been expressly approved by the EC Commission as indispensable to the marketing of its products. YSL provided significant financial support to its retailers, for example by providing show cards, samples, tester stands and merchandisers and by contributing to the costs of beauty consultants (to a significantly greater extent in the UK than on the Continent). Retailing costs did not inhibit the scope for competition between retailers within the authorized network and this might increase now that the quantitative limit on their numbers had been abandoned.

Stockholding requirements

7.148. YSL drew attention to the justification in the EC Decision of its requirement that all its retailers should hold at least one product from two-thirds of its entire range, on the grounds of ensuring the availability to consumers of the main products in each of the ranges at each outlet. The need for this availability had been

urged on the EC Commission by consumer associations. If only better-selling fragrances were available, without the associated body products, this would take away what was perceived as the total world of a YSL fragrance.

7.149. The requirement that retailers should purchase annually at least 40 per cent of the average level of purchases by all UK outlets in the previous year had been explained by the EC Commission in terms of concentrating distribution on cost-effective retail outlets. The EC Commission had been concerned that the minimum turnover requirement should not be a means of effectively preserving a quantitative limit on the number of retailers. YSL pointed out that the figures of 40 per cent and two-thirds reflected reductions in its previous requirements agreed in the course of discussions with the EC Commission.

Level of prices to consumers

7.150. YSL said that consumers expected prices for fine fragrances to be high in relation to prices for mass fragrances, which were not sold on the basis of their aura and prestige, nor with the benefit of specialist advice. The fact that the volume of YSL sales in the UK had risen by 58 per cent between 1983 and 1990 suggested that consumers accepted its prices as reasonable for high-quality products sold with a high level of service.

Recommended resale prices

7.151. YSL said that the use of RRPs enabled it to position each of its brands in the market in relation to its other brands and to directly competing brands of other suppliers. RRPs also provided a useful indication to retailers of the level at which they could expect to sell a product competitively. However, retailers were free to sell YSL products at whatever price they chose. YSL did not normally monitor retail prices of its products, but for this inquiry it had carried out a random survey of 262 of its authorized outlets early in 1993 and had found 53 of them selling its Paris 50ml EDT natural spray below the RRP. There had also been price-cutting by a number of its authorized retailers in the period before Christmas 1992, at the time of year when sales peaked.

Consumer choice of outlets

7.152. YSL said that selective distribution was aimed at ensuring levels of retail service and ambience that were appropriate to the quality of its products, not high prices. If, however, some retailers were to be allowed to offer lower prices on the basis of a somewhat lower level of service and ambience, this would, in effect, permit those retailers to free-ride on others whose high level of service and ambience had helped to make the products attractive to the consumer. This would undermine the principle of selective distribution as approved by the EC Commission. There was plenty of competition between retailers and a choice between competing suppliers' brands at all authorized outlets.

Duty-free outlets

7.153. YSL said that duty-free outlets at airports compared very favourably with other authorized retail outlets. It had recently developed a contract for duty-free outlets which had very few differences from the standard form contract for domestic retailers. As sales through these outlets were subject to virtually the same requirements as sales through YSL's other authorized outlets, they were entirely consistent with YSL's selective distribution network. Travellers tended to associate duty-free purchases with the glamour of foreign travel. Sales through duty-free outlets did not in any way invalidate the justification for selective distribution.

Discrimination against retailers

7.154. YSL said that all the criteria it used for selecting retailers were objectively justified in order to achieve consistency between the quality and prestige of its products and the manner in which they were distributed, and had been accepted as such by the EC Commission. None of the criteria had been defined in a manner that discriminated unfairly against any type of retail outlet. YSL had appointed a single person to conduct all evaluations in the UK in order to avoid any inconsistency in the evaluation of outlets. Applicants for authorized status whose premises failed to meet the criteria were told the reasons and, if they wished, could receive a copy of the evaluation report. If the applicant, having seen the report, challenged the result, a further evaluation would be made. YSL was reviewing all existing outlets against the criteria in its new authorized retailer agreement; it was already apparent that a number of these would not meet the criteria and they were being given six months to make the improvements necessary if they wished to retain authorized status.

7.155. YSL said that it had evaluated the outlets for which Superdrug had sought authorization. It had informed Superdrug that it found them deficient in some respects, and although certain stores came close enough to the standards to be given an opportunity to bring them up to standard, YSL considered this inappropriate because it was concerned that other products in the stores, and their manner of sale, would detract from the YSL image and that public perceptions of Superdrug, as shown by an independent survey conducted by Taylor Nelson, were unfavourable to it as a retailer of YSL products. Some 68 per cent of those interviewed in the survey thought that they were less likely to consider YSL products exclusive if sold in Superdrug stores and 60 per cent thought that the prestige of YSL products would be diminished by being sold there. YSL told us that it would be willing to discuss the image problem with Superdrug and considered that the adoption of a different name for those stores from which Superdrug wished to sell fine fragrances might lead to a different conclusion if it changed consumers' perceptions of the stores.

7.156. YSL had agreed to evaluate 12 Tesco stores in respect of which authorization had been sought, but was waiting for Tesco to arrange the inspections. Meanwhile, it had asked Taylor Nelson to conduct a survey of the kind undertaken in relation to Superdrug and this had shown that, although Tesco was regarded as a high-quality food retailer, the majority of consumers did not regard it as an appropriate outlet for YSL products. Some 78 per cent of those interviewed thought that they were less likely to consider YSL products exclusive if they were sold in Tesco stores and 65 per cent thought that the prestige of YSL products would be diminished by being sold there.

7.157. YSL considered that its system contained adequate checks and balances to ensure fair treatment of retailers. It did not believe that there was a case for a system of independent arbitration, which it expected would add unduly to the costs and complexities of the procedures. An aggrieved retailer could apply to the OFT or to the EC Commission to have a grievance examined. The EC Commission had the ultimate sanction of withdrawing the benefit of an exemption decision and could, in appropriate cases, impose fines. There was a powerful incentive on suppliers to operate YSL/Givenchy-type systems in the manner intended by the EC Commission.

The grey market

7.158. YSL said that the adoption of a selective distribution network frequently gave rise to a grey market as retailers who failed to gain admission to the network sought to obtain supplies of the products. Such retailers were free-riders on the authorized retailers as they seldom accepted any of the costs and responsibilities of promoting and maintaining the prestige of luxury brands. Supplies to the grey market might originate from wholesale distributors who bought more than they needed for normal resale and sold the excess at a quick profit. YSL terminated supply contracts with wholesalers found to do this. Authorized retailers with cash flow difficulties sometimes sold products to unauthorized traders to generate cash. YSL had taken action on a world-wide basis to trace the sources of grey-market stock and prevent sales outside the network in future.

7.159. YSL considered that, while consumers might benefit in the short term from getting genuine fine fragrances more cheaply, there was a limited range of products, no guarantee of their condition, no advice from staff with product knowledge and in the longer term the image of the products would be debased.

Counterfeit and replica fragrances

7.160. YSL was concerned to prevent counterfeiting of its products, which was particularly a problem for brands which were market leaders. It was also concerned about replica fragrances and had taken legal action against one producer of such fragrances.

Superdrug advertising

7.161. YSL said that it had not attempted to dissuade any publishers of high-quality fashion magazines from accepting Superdrug advertisements for fine fragrances in their magazines. It placed advertisements in magazines which reflected the brand image it wished to project and if it felt that the advertising in a magazine was moving the magazine's image away from the brand it wished to advertise it would reconsider its use of that magazine.

Suppliers who did not attend hearings

Creative Fragrances Ltd

7.162. Comments were received from Creative Fragrances and from Parfums Rochas, whose wholly-owned subsidiary, Rochas Perfumes Ltd, is managed by Creative Fragrances in accordance with policies laid down by Parfums Rochas. Parfums Rochas' comments were similar to the following statements by Creative Fragrances.

Selective distribution

7.163. Creative Fragrances said that it attempted to ensure that the outlets selling its products had an environment in keeping with the luxury quality of the merchandise. Its aim in doing this was to protect the image of its brands.

Stockholding requirements

7.164. Creative Fragrances thought that any retailer which operated a successful perfumery business would stock a range of products consistent with the demand for those products. It did not stipulate any particular quantitative requirements.

Recommended resale prices

7.165. Creative Fragrances said that it recommended resale prices at the retailers' demand, so that they might ensure that their pricing strategy was competitive. Retailers were entirely free to set their own prices and these were not monitored. RRP's were less important than wholesale or invoice prices.

Consumer choice of outlets

7.166. Creative Fragrances believed that its selective distribution policy enhanced the sales of fine fragrances and could only have an adverse effect on consumers if the distribution were so limited that they were unable to make the purchase of their choice. This was not the case.

Discrimination against retailers

7.167. Creative Fragrances said that it had not refused to supply a retailer unless it considered that retailer to be an unacceptable credit risk. There were at present no outstanding requests from retailers for admission to its distribution network.

The grey market

7.168. Creative Fragrances said that it was relatively easy for retailers to obtain grey-market supplies of some of the more popular reference products and three of its brands had found their way into this market. It had advised its suppliers of this fact from time to time.

Lancaster Group Ltd

Selective distribution

7.169. Lancaster said that selective distribution was necessary to ensure that its products were sold through outlets which were compatible with the style and prestige of its products, with advice and assistance to consumers from suitably qualified staff.

Recommended resale prices

7.170. Lancaster said that it recommended resale prices to its retailers as a guideline. The retailer was entirely free to fix the actual retail prices. Lancaster knew that retailers were selling its products at below the RRP, although it did not have details.

Consumer choice of outlets

7.171. Lancaster said that its selective distribution system gave consumers a fairly wide choice of outlets from which to buy its products. There was strong competition between its authorized retailers.

Discrimination against retailers

7.172. Lancaster said that the criteria which it applied in deciding whether to supply retail outlets were set out in a new retailer agreement drafted to reflect the EC Commission Decisions. The criteria were made known to retailers. No decision had yet been taken on the application from Superdrug.

The grey market

7.173. Lancaster said that it thought the supplies of its products on the grey market stemmed mainly from traders in markets outside Europe. The grey market was interested only in products with a high turnover such as aftershave lotions and EDT. Lancaster was taking steps to prevent its products getting on to the grey market.

Nina Ricci (UK) Ltd

Selective distribution

7.174. Ricci said that selective distribution was essential to maintain the desirability of its products in consumers' eyes. If it were removed, fine fragrances would disappear from the market.

Stockholding requirements

7.175. Ricci recognized that the requirements on authorized retailers concerning level and spread of stock could add to costs. But they were necessary because consumers expected the product range to be available. The supplier, moreover, could not extend the requirements to unreasonable limits, or it would be forced to accept returns.

Level of prices to consumers

7.176. Ricci said that consumers considered the higher price of fine fragrances compared with mass fragrances to be justified by the aura of quality and exclusivity attached to the products. The margins of manufacturers, wholesalers and retailers could not be considered to be too high. There was ample competition at all levels of the fine fragrance market to ensure that this was not so.

Recommended resale prices

7.177. Ricci recommended prices to retailers, but they were free to sell at different prices and price competition was not restricted.

Consumer choice of outlets

7.178. Ricci considered that it would be unrealistic to allow some shops to sell fine fragrances at lower prices on the basis of a lower level of service and ambience. It would no longer be worthwhile to operate at the higher level of service and ambience and eventually fine fragrances would disappear or become mass-market products.

Duty-free outlets

7.179. Ricci believed that duty-free shops at airports met the normal requirements of authorized outlets. On boats and aircraft, expectations were different; consumers accepted that space was limited.

Discrimination against retailers

7.180. Ricci adopted a set of criteria for assessing retail outlets which were consistent and open and were applied universally. Applications from recognized duty-free outlets, which had to qualify against certain Customs criteria, were always accepted provided they had specific facilities for fragrance sales.

The grey market

7.181. Ricci believed that the grey market only existed because fine fragrances were desirable and exclusive. Abolishing selective distribution would destroy the grey market, but would also destroy fine fragrances. The grey market did not provide a net benefit to consumers as the benefits of lower prices were outweighed by limited product range, a lack of trained sales staff and the risk that products were not genuine or were in poor condition. Manufacturers should close loopholes in their distribution systems to deny the grey market supplies.

Superdrug advertising

7.182. Ricci denied exerting any pressure on the publishers of high-quality fashion magazines to refuse advertisements from Superdrug for cut-price fine fragrances.

Procter & Gamble (Cosmetics & Fragrances) Limited

Selective distribution

7.183. Procter & Gamble said that its policy in marketing and distributing fine fragrances had been to maintain the trading pattern it had inherited when it bought the business in 1991, while taking steps to bring the administration of its distribution system in line with the EC Decisions on the YSL and Givenchy systems. It sold its luxury fragrances through outlets which sold competing high-quality brands. Generalized distribution of the products could downgrade the image and exclusive character of the product, remove the element of luxury and in the long term reduce the demand.

Retailers' costs

7.184. Procter & Gamble said that the EC Decisions recognized that requirements such as specialized advice at point of sale, a suitable display of products, and stock rotation and promotion improved the distribution of fine fragrances and benefited the consumer. It did not consider that it imposed requirements on retailers which were more onerous than was necessary to attain these objectives.

Stockholding requirements

7.185. Procter & Gamble pointed out that obligations on authorized retailers to stock at least two-thirds of the whole range of a particular product and to make minimum annual purchases were regarded in the EC Decisions as contributing to improved distribution of fine fragrances and benefiting the consumer. Procter & Gamble believed that such obligations were aimed at ensuring continued consumer choice and that, if such requirements were prohibited, it would probably be uneconomic for most suppliers to maintain an entire product range for a particular line.

Recommended resale prices

7.186. Procter & Gamble thought that price was an important element of marketing and business strategy because it influenced the potential sales volume of the brand. Its main reason for recommending prices to retailers was to encourage them not to price a product too high. If an item were too highly priced, the volume would probably decline and this would have an adverse effect on the appeal and potential of the brand. Procter & Gamble did not systematically monitor retail prices and was not concerned if retailers sold below the RRP, providing that the products were sold in a manner which reflected the prestige of the product.

Consumer choice of outlets

7.187. As an extensive variety of brands were sold in a large number of outlets Procter & Gamble did not think that selective distribution reduced consumer choice. The fact that the products tended to be sold in outlets with a prestigious image helped to preserve the exclusive character of the products which was an essential factor in competition.

Discrimination against retailers

7.188. Procter & Gamble said that it was formulating qualitative criteria for selection of retailers in accordance with the EC Decisions and would seek to apply them in a fair and non-discriminatory manner to all retailers who wished to sell its products. On the rare occasions when a new application to retail the products was received, it was referred to the President of Eurocos Cosmetic GmbH. The only instance of its having postponed a decision to supply a retailer was in the case of a Superdrug store and this had been due to the fact that it was still in the process of finalizing its formal criteria.

7.189. Procter & Gamble considered that UK competition legislation offered suitable remedies to an aggrieved retailer. Articles 85(1) and 86 of the EC Treaty created direct rights which were enforceable in national courts and the EC Commission had published a notice to encourage greater use of EC competition rules in national courts. Procter & Gamble therefore believed there was no need for the creation of a new remedy in the form of arbitration.

The grey market

7.190. The grey market was a largely foreseeable consequence of a selective distribution system. Procter & Gamble believed that its growth and the existence of unauthorized retailers would damage the image of fine fragrances. Because these outlets often offered poor levels of service consumers might experience problems in product availability and continuity and might receive inaccurate information.

Superdrug advertising

7.191. Procter & Gamble had never been involved in any discussions with publishers to discourage them from accepting advertisements from Superdrug or any other company.

Revlon International Corporation

Selective distribution

7.192. Revlon said that it operated a selective distribution policy because, by definition, fine fragrances appealed only to a small niche market of customers, and therefore there was insufficient volume to achieve a wide distribution profitably. It was a question of economies of scale and small retailers did not want to stock a wide variety of brands. They only wished to stock brand leaders and this did not include Revlon's fine fragrances.

Recommended resale prices

7.193. Revlon said that it recommended prices to retailers to reflect their required margin over trade price. Trade prices were set according to manufacturing costs and positioning to achieve the required return on investment.

Discrimination against retailers

7.194. Revlon had no written procedure for deciding which retailers to supply. When evaluating an outlet it would consider whether the style of the premises reflected the prestige of the brands and the ability to achieve sufficient sales to make the outlet viable. Consistency was ensured by the Sales Director reviewing the evaluation and making the final decision in all cases.

The grey market

7.195. A few Revlon products had been sold into the UK grey market from the USA. The quantities had been very small, probably because there was little or no demand for them. Because the grey market had minimal effect on Revlon brands it had taken no steps to prevent this from happening.