LEWIS SILKIN

Routes to Market Series: A to B via the four Cs

Getting goods from A to B can be a tricky task, particularly when those goods are being sold across borders. There's a lot to think about: from broad issues, like how to structure your supply chain to ensure the greatest level of efficiency, to the nitty gritty of how much import duty to pay when your goods arrive at their destination.

In the UK, the positions on competition law, consumer law, and customs taxes originally stem from EU legislation; however, since Brexit (and throughout 2024, even despite the early general election), the UK government has introduced legislation which cements the UK's reputation as an exciting place to do business, including, for example, the introduction of the Digital Markets, Competition and Consumers Act (which aims to regulate competition in digital markets and provide additional protections for consumers).

Here at Lewis Silkin, we're well-versed in the nuances of these new pieces of legislation, as well as being commercially astute, business-focussed partners to some of the biggest players at all levels of the supply chain. Indeed, we've helped countless businesses to navigate the regulatory requirements of establishing and maintaining their routes to market into the UK and, in this series of articles, our experts discuss some of the key topics which you might want to consider when doing the same.

Contracting

There are many different routes to getting a product to market. From simple supply chains where a sole proprietor has limited suppliers and a single retail outlet, to complex supply chains involving multiple retail outlets, outsourced manufacturing, outsourced marketing and distribution, along with a web of suppliers and a network of logistic providers.

The right supply chain set-up and the different contracting considerations will depend on a business' objectives and growth trajectory. As a business grows, it is important to fully understand the supply chain building blocks that are being put in place and how they can be properly managed.

Since the UK left the EU, the free movement of goods has been a hot topic. EU brands, distributors and exportors have a new raft of issues to contend with from UK competition law to customs regulation. Robust and well understood contracts lie at the heart of a successful relationship, and importantly, the parties having clarity on the commercial and legal parameters of that relationship.

So, what are some of the basics you need to think about?

1. Key supply chain participants and contracts

The supply chain process usually starts with procuring raw materials and arranging the manufacture of a product. In terms of contracts, businesses may need to consider manufacturing or co-manufacturing agreements, outsourcing and subcontracting agreements, and other supply agreements.

Logistics (and reverse logistics) partners may also come into play where products need moving through the supply chain, often across multiple jurisdictions. Warehousing providers that can also provide associated services (such as inventory management, quality control, storage in bond) may also be important.

Further down the supply chain, businesses may need to consider sales-related partners, such as agents and distributors/resellers (considered in more detail in 2 below) and franchising arrangements (which is a particularly common model used in the food and beverage sector to bring products to market).

2. Outsourcing marketing and distribution

Particularly when expanding into new jurisdictions, many businesses choose to outsource the marketing and distribution of products to an agent or distributor/reseller. Sometimes, this is because the laws in a certain jurisdiction require that sales are made through a local agent or distributor. However, it might also be a quick way to enter into new markets, saving cost on setting up selling operations and making the most of an agent/distributor's local connections and knowledge.

When it comes to the outsourcing of marketing and distribution, businesses should fully understand the nuances of the different options as there can be significant legal implications.

What's the legal difference between an agent and a distributor?

An agent acts on behalf of its principal and can either introduce a customer to the principal or it can arrange for a contract to be entered into between the principal and customer. Agents aren't usually a party to the contract between the principal and customer and goods will normally pass directly from the principal to the customer. An agent tends to be paid commission on sales it helps its principal achieve. Usually, there will only be one contract that the agent is party to and that is the contract between the agent and principal setting out how the arrangement will work.

In contrast, a distributor is an independent trader that usually buys products from the principal and resells them on to its own customers. This means, usually, there will be two contracts the distributor is a party to - one between the distributor and principal (for the purchase of the products), and one between the distributor and its own customer (for their resale).

Which arrangement is better?

Which arrangement is better will depend on the circumstances and objectives. A distributor is essentially just a reseller of products so, if keeping close control over the marketing and sale of products is the objective, an agency relationship may be preferred but this kind of arrangement tends to require more leg work and can have a significant financial impact when the relationship ends.

In many counties (particularly in the EU and UK), agents might be due a potentially significant lump sum payment when an agency agreement comes to an end. Businesses considering utilising a commercial agent will therefore need to think carefully about the relevant legal, financial and tax implications. Businesses should also ensure any contract underpinning the agency relationship complies with agency laws and mitigates risk as much as is possible.

Competition law should be at the forefront of any decision, particularly in respect of distribution arrangements where territorial exclusivity is in scope.

3. Managing the supply chain

It is essential to create and maintain the right contractual framework to protect the supply chain and business interests. From a contractual perspective, just a few of the key issues to consider are set out below.

Regulatory compliance

There are increasingly complex local and international regulatory considerations to take into account across a global supply chain. Contracts across the supply chain may need to address bribery and corruption issues, modern slavery and human trafficking, environmental concerns, cyber security, product safety and liability, import/export requirements as well as industry specific regulation.

Brexit has had a significant impact on import and export custom controls.

Risk management

Supply chain contracts should address how to deal with unanticipated issues to protect the resiliency of the supply chain. This may include consideration of, amongst other things, insurance, incident response, geo-political risk, supplier delivery capability, labour shortages or price increases, product and component recalls, supplier disputes. At a basic level, contractual provisions that prevent, mitigate or shift risk will be vital.

Brand protection

Brand protection can present a difficult challenge particularly across a global supply chain. Each link in the supply chain should include appropriate intellectual property contractual protection to protect the value in a brand but also the overall strength of the supply chain.

Exit

The contractual provisions around exiting an arrangement in the supply chain should be carefully planned. Flexibility may be needed but resilience of the chain will also be paramount. A break or fault in just one link can cause much wider repercussions in the broader supply chain.

Getting your supply chain set-up right, particularly in the context of a rapidly growing business, can present significant challenges. Choosing the appropriate structures and contractual protections will be essential for a successful, resilient and scalable route to market.

Competition

When appointing a distributor, it is vital to ensure that the distribution agreement complies with competition law. Getting this wrong can result in significant fines and lead to reputational harm.

Vertical agreements

In competition law parlance, a distribution agreement is what is known as a 'vertical agreement'. This is because it is made between a supplier and a distributor operating at different levels of the supply chain. The supplier sells down to the distributor and the distributor sells on to retailers or consumers further down the chain.

Distribution arrangements can be complex. A supplier may operate an exclusive distribution system, a selective distribution system, an open distribution system, or a combination of these. If it has granted some degree of territorial exclusivity to a particular distributor, it will want to

limit other distributors' access to that territory. It will also want to protect its brand by ensuring that its distributors are meeting certain quality standards and by restricting how its distributors may work with competitor brands or other, unauthorised distributors.

However, certain obligations and restrictions can go too far and breach competition law. So, it is important to ensure that the contractual obligations and restrictions are drafted carefully to ensure they are compatible with applicable competition laws. This has been complicated somewhat by Brexit because suppliers appointing a distributor in the UK may need to take into account both the UK and the EU competition law regimes.

There are some red lines that cannot be crossed, such as granting absolute territorial protection to a distributor or imposing fixed or minimum resale prices. These are examples of practices that competition authorities consider so injurious to competition as to justify significant fines, regardless of their actual effects on competition. Fines for breaching UK competition law can be up to 10% of worldwide turnover for the previous business year.

Safe harbour

Helpfully, competition law takes into account that some vertical agreements may have little or no real impact on competition. Under both UK and EU regimes, there is a 'safe harbour' available where the parties involved do not have a significant share of the relevant market and where the agreement between the parties does not contain certain 'hardcore' or 'excluded' restrictions.

In the UK, this safe harbour is set out in the Competition Act 1998 (Vertical Agreements Block Exemption) Order 2022 ('VABEO'). To fall within the scope of the UK safe harbour, the parties and the agreement must meet certain cumulative conditions. The conditions are set out in the VABEO but are explained in more detail in the CMA Guidance on the Vertical Agreements Block Exemption Order ('CMA Guidance'). Although the CMA Guidance is non-binding, it is nevertheless a very important aid to understanding whether an agreement may be protected by the VABEO and should always be considered alongside the VABEO.

Broadly, the conditions are as follows:

1. The market share of each party must not exceed 30%

This means that the supplier's share of the market on which it sells the goods must not exceed 30% and the distributor's share of the market on which it buys the goods must not exceed 30%. Below the 30% level, there is a presumption that the parties lack market power and that the agreement between them will not affect competition. Assessing a party's market share can be a complex process because this requires a detailed analysis of the relevant product and geographic markets and it often requires input from econometrists.

It must also be remembered that the VABEO is only intended to apply to 'vertical agreements', i.e. between parties operating at different levels of the supply chain. Consequently, it would not apply to an agreement between competitors as that would be treated as a 'horizontal agreement'. However, subject to certain conditions, the VABEO can apply to 'dual distribution', which is where a supplier sells both through its own sales outlets and through independent distributors. The VABEO will only apply to dual distribution in certain non-reciprocal situations, such as where the supplier is either a manufacturer, wholesaler or importer and is also a distributor of goods, while the buyer is only a distributor that does not compete with the manufacturer, wholesaler or importer at the relevant upstream level.

2. The agreement must not contain 'hardcore restrictions'

If the agreement contains so-called hardcore restrictions, the entire agreement loses the benefit of the safe harbour. Hardcore restrictions would include resale price maintenance obligations which require a distributor to sell at prices specified by the supplier and total export bans preventing a distributor from selling to customers outside their designated territory. There are some significant watchouts to be aware of:

Price fixing or resale price maintenance: The VABEO treats resale price maintenance as a hardcore restriction. This will apply to any agreement or practice requiring a distributor to adhere to price levels set by the supplier. A supplier may impose a maximum resale price or a recommended resale price, as long as these don't equate to fixed prices – the distributor must always be free to set its own prices.

Territorial/customer restrictions: The general principle is that a distributor must be free to decide where and to whom it sells the contract goods and any restriction on this is considered a hardcore restriction. However, the VABEO provides certain exceptions to this principle which vary depending on whether the supplier is operating an exclusive, selective or open distribution system. For example, where a supplier operates a selective distribution system, it can prohibit a distributor from making active sales or passive sales to unauthorised distributors located in the geographical area where the supplier operates the selective distribution system. In an exclusive distribution system, where a supplier has reserved a territory to one or more exclusive distributors, it can restrict other distributors from making active sales into the reserved territory but it cannot restrict passive (i.e. unsolicited) sales into that territory. Generally speaking, there are very few circumstances in which it is lawful to restrict

distributors from making passive sales so, if an agreement contains a restriction on passive sales, this will require very careful consideration.

Parity obligations: The VABEO defines a 'wide retail parity obligation' as a restriction ensuring that the prices (or other terms) at which a supplier sells its goods on a sales channel (online or offline) are no worse than those offered by the supplier on another channel. The VABEO treats wide retail parity obligations as hardcore restrictions. By contrast, narrow retail parity obligations which apply only to the supplier's direct sales channels (e.g. its own website) can benefit from the safe harbour.

3. The agreement must not contain 'excluded restrictions' that cannot be severed

If the agreement contains excluded restrictions, these restrictions will fall outside the safe harbour but the rest of the agreement can still benefit. In the UK, non-compete clauses that are tacitly renewable beyond five years will be considered 'excluded restrictions' and will fall outside the scope of the safe harbour. This is because they are deemed to be concluded for an indefinite period.

Excluded restrictions also include obligations preventing a distributor from dealing in any goods after termination and obligations preventing a member of a selective distribution system from selling the brands of particular competing suppliers.

If the conditions set out in the VABEO are met, an agreement can benefit from the safe harbour. However, it is important to remember that vertical agreements that do not satisfy the conditions are not automatically in breach of competition law. Instead, they must be considered on a case-by-case basis to assess their pro-competitive and anti-competitive effects by reference to all the relevant circumstances.

Finally, even when appointing a distributor in the UK, it is essential to consider whether the agreement might have an effect on trade in the EU. This is because EU competition law has extra-territorial effect. If so, it will be necessary to factor in EU competition law – which is stricter in some areas and less so in others – and, if possible, to draft the agreement to comply with the requirements of the EU safe harbour.

Consumer

Businesses intending to sell goods to consumers in the UK will need to ensure they are doing so in a way that is compliant with UK consumer laws. UK consumer laws are complex and are set out in a number of different pieces of legislation, including under the Digital Markets, Competition and Consumers Act ("DMCCA"), and so it is important to think carefully about what laws will apply and how.

So, what do you need to think about?

1. Who are you selling to, where are you selling it and what are you selling?

Who you are selling to

Firstly, businesses should consider who they are selling to. Where an individual is contracting as a consumer, they will benefit from extensive protections under UK consumer laws. The legal position and contracting rules that apply to business-to-consumer interactions are very different from those that apply to business-to-business interactions. It isn't always straightforward assessing whether you are dealing with a consumer or not – for example, what is the position if you are intending to sell to your own employee, or where an individual is buying a phone that they intend to use for sending work emails but also for personal use?

Businesses selling to both consumers and businesses will need to think carefully about how they structure the sales journey to ensure the relevant rules are being met.

Where you are selling

Different consumer rules will apply depending on how a sales contract is made. If sales are made online or by phone, the position will be different to that where sales are made in a bricks and mortar shop.

What you are selling

Different consumer rules and exemptions also apply depending on exactly what is being sold (e.g. services, goods, digital content). Again, this isn't always a straightforward assessment. For example, smart home devices like security cameras might only appear to be "goods" but they are often sold in combination with an integrated subscription service. Subscription services are governed by additional rules under the DMCCA which may need to be taken into account.

2. Have you got legal documents in place?

Once it is clear what rules apply, businesses should think about what legal documents need to be in place.

There are strict rules around how, what and when information needs to be provided to consumers. In practice, businesses will look to address a lot of these information requirements in legal terms and conditions and/or through policies such as a delivery and returns policy.

Failing to provide the right information, in the right form, and at the right time could be a breach of UK consumer laws, which can have practical as well as legal ramifications. For example, if a consumer has a 14-day statutory right to cancel a contract (i.e. the "cooling-off period", being the right to cancel a contract, for any reason, within 14 days of when the contract is entered into) and a business fails to tell a

consumer about this right in the correct way, the cancellation right could be extended by 12 months.

3. What does the consumer journey look like?

There is a lot more to complying with UK consumer laws than just having the right legal documentation in place.

UK consumer law applies to the whole lifetime of a trader-to-consumer transaction. Businesses therefore need to consider their commercial practices carefully, in the round.

Businesses should be aware that there is a lot of regulatory scrutiny around non-compliant consumer journeys. For example, the Competition and Markets Authority (the "CMA", the UK consumer law regulator) has recently shown a lot of interest in the use of:

- green claims (e.g. saying a product is "green" or "sustainable");
- harmful online choice architecture (also known as "dark patterns", e.g. manipulative online designs such as the use of countdown clocks to create a sense of false urgency);
- fake reviews (e.g. supressing negative customer reviews or manipulating consumers to submit a positive review); and
- subscription traps (e.g. recurring subscriptions a consumer may take-up wrongly assuming they are making a one-off purchase or redeeming a free offer).
- Businesses should objectively and critically consider the practices they employ and associated consumer journeys to avoid falling foul of consumer laws and attracting regulatory focus.

4. What happens if you get it wrong?

The consumer protection law enforcement regime has significantly changed under the new DMCCA. Under the DMCCA, the CMA will be able to enforce consumer protection law directly (rather than having to take each case to court) and it will be able to impose fines of up to the greater of £300,000 or 10% of an infringing business' global turnover.

With huge new fines on the table, the risks of getting it wrong are higher than ever. Consumer law risks should firmly be on the agenda of every consumer-facing business' board.

Customs

A crucial element of ensuring the smooth running of an international supply chain is for a business to make sure they are compliant with local customs legislation. If you don't comply, your goods could become stuck at borders.

From a cost perspective, you should also bear in mind that you may be required to pay import duty as well as import VAT (or the local equivalent) when you bring goods into a country for onward sale.

So, what are some of the things you need to consider before bringing goods into GB?

1. What administrative obligations do you have?

Depending on where the goods are being imported from, safety and security declarations will need to be submitted before the goods arrive in GB. This is in addition to the customs declaration that will need to be submitted for the goods on their arrival into GB. It is in the customs declaration that you will declare to HMRC which customs procedure you want to apply to the goods being imported – i.e. will they go into free circulation for sale immediately or do you want a 'special customs procedure' to apply to them instead.

2. What happens at the border?

On arrival in GB, goods need to be 'presented' to border control – if they aren't then they will be liable to forfeiture. HMRC can inspect the goods, verify the data logged about them and raise enquiries about the goods once they are imported into GB (and before they are released into free circulation).

3. Will tax be payable at the border?

In GB, the liability to pay import duty etc is typically triggered when goods are released into free circulation.

The amount of import duty etc payable will depend on:

the customs tariff classification of the good imported;

- the value of the imported good;
- the country of origin of the good; and
- if a preferential duty rate applies to the good import into GB by virtue of (for example) a free trade agreement entered into by the UK.

4. Who is liable to pay the tax?

You would typically expect the importer to be liable to pay import duty on goods brought into GB. This can be affected however if the importer chooses to engage a representative to fulfil their administrative obligations in respect of the import on their behalf – in particular, if the representative is acting as the importer's indirect representative.

5. How can the sales contract impact the parties' customs obligations?

Where goods are sold and bought internationally between businesses (i.e. a bike is manufactured in Germany and sold to a UK business), consideration should be given to any Incoterms entered into by the parties prior to the import of the goods into GB. Incoterms set out which party will be responsible for specific actions on the international sale of goods.

6. What about special customs procedures?

There are a variety of special customs procedures a business might choose to make use of when bringing goods into GB (instead of immediately bringing those goods into free circulation). These include the storage procedure whereby goods can be held in a specific storage facility when they are imported into GB before they are released for free circulation. Use of the storage procedure can help delay when import duty is payable by an importer.

Each special customs procedure has specific requirements that need to be met for a business to qualify for them. These requirements should be checked before goods are brought into GB if you want those goods to benefit from them.

7. What are the risks of getting it wrong?

If HMRC disagrees with a customs declaration on inspection of the goods imported at the border, they can seize those goods pending payment of the correct amount of import duty for them. After the goods have been released into free circulation, HMRC can also raise a C18 post clearance demand note (if they believe that there has been an underpayment of import duty) requiring the importer to pay such underpayment of duty.