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EU CONSULTS ON NEW EU COMPETITION POLICY FOR DISTRIBUTION AGREEMENTS

To Our Clients and Friends:

On 18 December 2020, the European Commission (the “Commission”) launched a comprehensive public consultation (the “Consultation”) on the revision of the European Union (“EU”) antitrust rules specifically applicable to distribution agreements, namely, the 2010 *Vertical Block Exemption Regulation* (Regulation 330/2010 or “*VBER*”) and the 2010 *Vertical Guidelines*, both of which will expire on 31 May 2022.[1]

The Commission is consulting with a view to gathering feedback on a number of policy options:[2]

- On one side, the Commission proposes to adopt an arguably more *lenient* approach to the application of EU competition rules to certain types of vertical arrangements, ranging from: **long-term non-compete obligations**, **efficiency-generating resale price maintenance (“RPM”)**, **sustainability agreements in the context of the European Green Deal**,^[3] **active sale restrictions outside of pure exclusive distribution**, and **measures indirectly restricting online sales**.
- On the other side, the Commission is considering adopting a *stricter* competition law enforcement strategy in relation to other types of vertical agreements such as: **restrictions on price comparison websites** and on **online advertising**, **dual distribution** and **parity obligations** (e.g., most favoured nation, or “MFN” clauses).

The Consultation is open until 26 March 2021, and will be followed by a report on the findings and results of the impact assessment phase. This will result in the publication of the proposed new draft *VBER* and accompanying *Vertical Guidelines*. Given the range of policy options under consideration by the Commission, this Consultation gives companies involved in both traditional and online retail business a unique opportunity to seek to influence the shape of future vertical restraint policies.

1. Background & Historical Context

Since the 1960s, the Commission has had in place regulations and guidance exempting certain categories of distribution agreements from the application of EU competition rules prohibiting anti-competitive agreements or arrangements.[4] The current *VBER* entered into force on 1 June 2010.

The *VBER* block exempts from the application of EU competition law distribution agreements where the market shares of the supplier and reseller do not exceed 30% in the respective relevant markets. The exemption applies if the agreement does not include so-called ‘hard-core’ restrictions.[5] Where companies cannot safely determine that their distribution agreement is covered by the *VBER* ‘safe harbour’, the company will need to consider: (i) if the agreement contains any ‘hard-core’ or excluded restrictions, (ii) if it may have any foreseeably anti-competitive effects on competition, and (iii) if there

are any efficiencies that may benefit the agreement from an individual exemption under Article 101(3) *TFEU*. The *Vertical Guidelines* provide guidance to companies to perform these individual assessments.

2. The 2010 *VBER* and *Vertical Guidelines* and the Commission’s Approach to E-Commerce and Other Restrictions

The *VBER* and the *Vertical Guidelines* currently in force include rules and guidance that aim at fostering cross-border trade and online commerce as well as promoting competition. For example, the 2000 *Vertical Guidelines* allowed suppliers to require that quality standards be met in order to allow the resale of products through a distributor’s website.[6] The 2010 version of the *Guidelines* implicitly limited the application of such quality standards in the context of the Internet to situations involving selective distribution arrangements. And in any event, the standards had to be applied in an “overall equivalent” manner to both physical and online points of sale (*i.e.*, stricter standards could not be applied only to online sales).[7] The 2010 *Vertical Guidelines* also set out a list of obligations and restrictions that suppliers were not permitted to impose on online resellers without potentially breaching EU competition law.[8]

The application of antitrust rules to e-commerce was significantly influenced by the 2011 Judgment of the Court of Justice of the EU (“CJEU”) in *Pierre Fabre*, which found that EU competition law prohibited manufacturers from engaging generally in online sales restrictions. In *Pierre Fabre*, the restriction resulted from the obligation on distributors to sell personal care products only in the presence of qualified pharmacists, *de facto* excluding sales through distributors’ websites.[9] The CJEU fully endorsed the view that e-commerce constituted a legitimate channel for the resale of products, and that a prohibition of e-commerce sales amounted to a hard-core restriction of competition ‘by object’. *Pierre Fabre* was followed by other decisions at EU and national level which confirmed the strict approach of European competition authorities and courts against measures likely to restrict e-commerce.[10]

By 2017, however, the Commission and the CJEU had started to become more nuanced in their approach to e-commerce, in particular regarding the sale of goods in online marketplaces. In the Commission’s final report in its *E-Commerce Sector Enquiry*, the Commission considered the perceived erosion of manufacturers’ freedom to limit online sales, and concluded that suppliers’ restrictions on distributors which made sales on online marketplaces were not *per se* anti-competitive.[11] Later that year, in *Coty*, the CJEU confirmed that manufacturers of luxury goods could seek to preserve the luxury image of those goods by preventing their sale in online marketplaces.[12]

3. The Commission’s Review of the *VBER* and the *Vertical Guidelines*

Against the backdrop of the findings of the *E-Commerce Sector Enquiry* and the *Coty* judgment, in 2018 the Commission launched a review of the 2010 *VBER* and the *Vertical Guidelines*, which are due to be replaced by 31 May 2022.

The first part of the review process lasted through September 2020, with the Commission gathering evidence on the functioning of the current *VBER* and the *Vertical Guidelines*. Respondents indicated that both the 2010 *VBER* and the *Vertical Guidelines* had to be revised, especially in light of the profound impact of e-commerce and digitalisation, the increase in direct sales by manufacturers to customers, the

wider use of retail price parity clauses, and the emergence of online platforms. Furthermore, the Commission found that there are certain practices and restrictions that have become more commonplace over the past few years, for which additional guidance is required (*e.g.*, dual distribution, online platform bans and restrictions on the use of price comparison websites).[13]

4. The Commission's Ongoing Impact Assessment

On 23 October 2020, the Commission published a Roadmap[14] for an impact assessment of the initiatives tabled to address the deficiencies identified in the 2010 *VBER* and *Vertical Guidelines*, identifying the following priorities:

1) The need to clarify, simplify and complete EU competition rules applicable to vertical agreements regarding:

- the assessment of possible **efficiencies resulting from resale price maintenance (“RPM”)**, which is currently a hard-core restriction under the *VBER*.
- how to address restrictions that have become more prevalent since 2010 (*e.g.*, restrictions on the **use of price comparison websites, or online advertising restrictions**).
- the treatment of new market players, such as **online platforms and marketplaces**, especially in areas of distribution not addressed by the current case law, such as agency agreements and dual distribution (*i.e.*, situations in which a supplier sells its goods or services directly to end customers, thereby competing with its distributors at the retail level).
- the objectives of the **European Green Deal**,[15] in relation to agreements pursuing sustainability objectives.

2) Non-compete clauses: These include obligations imposed on buyers not to manufacture, purchase, sell or resell goods or services which compete with those of the supplier, and are currently block exempted by the *VBER* provided that, *inter alia*, their duration does not exceed five years and is not automatically renewable. The Commission will consider a more lenient treatment of non-compete clauses whose duration may exceed this period due to automatic extensions, provided that they are subject to termination rights or renegotiation obligations.

3) Dual distribution: This occurs where a supplier sells its products to consumers both directly and through independent resellers. The growth of online sales has led to a significant increase in dual distribution practices, leading the Commission to consider issues such as: (i) horizontal competition concerns arising from suppliers' activities in the same market as resellers; (ii) the ability of dual distribution to satisfy the test for efficiencies that is used under Article 101(3) *TFEU*; and (iii) the comparison of the supplier's situation with that of other wholesale distributors and resellers which are not in a position to benefit from the *VBER* in comparable situations.

To address the more widespread use of dual distribution, the Commission has identified the following policy options (with the possibility of Options 2 and 3 being introduced in combination):

- *Option 1*: baseline scenario (*i.e.*, no policy change).
- *Option 2*: limiting the scope of the exemption to situations that are not likely to raise horizontal concerns by, for example, by introducing a threshold based on the parties' market shares in the retail market, and by aligning the exemption with what is considered to be capable of being exempted in the case of agreements among competitors.[16]
- *Option 3*: extending the exemption to dual distribution practices by wholesalers and/or importers.
- *Option 4*: removing the exemption from the *VBER*, thereby requiring an individual assessment under Article 101(3) *TFEU* for all dual distribution cases.

4) Active sales restrictions: The *VBER* treats as 'hard-core' situations where a supplier restricts the territory into which, or the customers to whom, a reseller can sell the products. Resellers should generally be allowed to approach direct individual customers ('active sales') and to respond to unsolicited requests from individual customers ('passive sales'). However, the current rules permit restrictions on active sales in limited cases, notably where they are justified to protect investments made by exclusive distributors.

The rigidity of the current *VBER* framework regarding the treatment of active and passive sales can render it difficult for suppliers to implement distribution networks that are tailored to their specific needs. For example, the *VBER* and the *Vertical Guidelines* do not foresee the use of 'shared exclusivities' between two or more distributors in a particular territory (*i.e.*, shielded from active sales by distributors established outside of their territory), or the genuine combination of exclusive and selective distribution methods for the same product lines in the same territory.[17]

The Commission has therefore identified the following policy options (with Options 2 and 3 possibly being introduced in combination):

- *Option 1*: baseline scenario (*i.e.*, no policy change).
- *Option 2*: expanding the existing exemptions available for the prohibition of active sales in order to give suppliers more flexibility to design their distribution systems.
- *Option 3*: ensuring more effective protection for selective distribution systems, by allowing restrictions on sales made from outside the allocated selective distribution territory to unauthorised distributors inside that territory.

5) Indirect measures restricting online sales: As noted above, most restrictions on distributors to sell through the Internet are considered to be 'hard-core' restrictions, which will generally not benefit from the automatic exemption under the *VBER*.^[18] The current versions of the *VBER* and the *Vertical Guidelines* apply the same approach to certain indirect measures that might hinder online sales, such as charging the same distributor a higher wholesale price for products intended to be sold online than with respect to products sold off-line ('dual pricing'), or where selective criteria are imposed for online sales that are not truly equivalent to the criteria imposed in brick-and-mortar shops (the "overall equivalence" principle).

The Commission recognises that, by not allowing suppliers to charge different wholesale prices depending on the actual costs of maintaining different channels, the current rules may prevent them from incentivising associated investments, notably in physical stores.

As a result, the Commission has identified the following policy options (with Options 2 and 3 possibly being introduced in combination):

- *Option 1*: baseline scenario (*i.e.*, no policy change).
- *Option 2*: no longer treating dual pricing strategies as a ‘hard-core’ competition restriction, with certain safeguards to be defined in accordance with principles established under case law.
- *Option 3*: no longer considering as a ‘hard-core’ restriction the imposition of selective criteria for online sales that are not “overall equivalent” to the criteria imposed in brick-and-mortar shops, with safeguards to be defined in accordance with principles set forth under case law.

6) Parity obligations (so-called ‘most-favoured nation’, or “MFN”, clauses): These types of clause require a business to offer the same or better conditions to its contracting party as those it offers to any other party, or by the company itself through its direct sales channels. Parity obligations are generally block exempted under the conditions of the *VBER*. However, the increase in their use, notably by online platforms, has led to the identification of possible anti-competitive effects under certain scenarios (*e.g.*, obligations that require parity with other indirect sales or marketing channels).

In order to address these scenarios, the Commission has identified the following policy options:

- *Option 1*: baseline scenario (*i.e.*, no policy change).
- *Option 2*: removing the benefit of the *VBER* and including within the list of excluded restrictions (Article 5 *VBER*) obligations that require parity relative to specific types of sales channel – thereby requiring an individual effects-based assessment of such obligations under Article 101 *TFEU*. For example, the benefit of the *VBER* could be generally excluded for parity obligations that relate to indirect sales and marketing channels, including online platforms and other intermediaries.
- Conversely, parity obligations relating to other types of sales channel would continue to benefit from the block exemption, on the basis that they are more likely to create efficiencies that satisfy the conditions of Article 101(3) *TFEU*.
- *Option 3*: removing the benefit of the *VBER* ‘safe harbour’ for all types of parity obligations, by including them in the list of excluded restrictions (Article 5 *VBER*). This option would require companies to perform an individual effects-based assessment in all such cases.

5. The Consultation – A Call for Action

With the release of its Consultation on 18 December 2020, the Commission is seeking to address the wide range of issues described above and to prepare for the adoption of a revised *VBER* and *Vertical Guidelines* in 2022.

While some of the issues addressed in the Consultation have long been highlighted by antitrust agencies, practitioners and industry stakeholders, a number of other issues have also raised heightened attention because of the extra impetus enjoyed by e-commerce during the last years.

The issues and potential solutions identified by the Commission in the Consultation (which is open until 26 March 2021) are important for manufacturers and resellers of all products, but especially for consumer products. Companies may therefore wish to take this opportunity to try to shape the future form of the EU competition rules which will apply to their distribution arrangements.

[1] The Consultation is available in the following link: <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12636-Revision-of-the-Vertical-Block-Exemption-Regulation/public-consultation>.

[2] These issues and policy options were first set out in the *VBER*'s inception impact assessment, published on 23 October 2020. See Ref. Ares(2020)5822391 – 23.10.2020, available at: <https://ec.europa.eu/info/law/better-regulation/>.

[3] The European Green Deal is the EU plan to create a sustainable economy, and provides for an action plan to boost the efficient use of resources by moving to a clean, circular economy, and to restore biodiversity and cut pollution. See further: https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.

[4] Article 101(1) *TFEU* prohibits all agreements or concerted practices that have as their object or effect the restriction of competition where the effect of that restriction may affect trade between Member States.

[5] See Article 4 of the *VBER* for a list of 'hard-core' restrictions. The *VBER* also identifies a limited number of restrictions which, if contained in a vertical arrangement, do not benefit from the *VBER* 'safe harbour' but which do not preclude the application of the *VBER* 'safe harbour' to the rest of the agreement (provided that the other conditions set out in the *VBER* are fulfilled).

[6] See *Commission notice – Guidelines on Vertical Restraints*, OJ C 291, 13 October 2000, pp. 1-44, para. 51.

[7] See *Vertical Guidelines*, para. 54.

[8] See *Vertical Guidelines*, para. 52.

[9] See Case C-439/09 *Pierre Fabre Dermo-Cosmetique* EU:C:2011:649.

[10] For more information, see A. Font Galarza, E. Dziadykiewicz, and A. Guerrero Perez, ‘Selective Distribution and e-Commerce: Recent developments in EU and national case law’, *e-Competitions Bulletin*, No. 63958, 2014. See further, *e.g.*, Case COMP/AT.40428 – *Guess*.

[11] See *Report from the Commission to the Council and the European Parliament, Final report on the E-commerce Sector Inquiry*, COM(2017) 229 final, 10 May 2017; and the accompanying *Staff Working Document*, SWD(2017) 154 final, 10 May 2017, Section 4.4.8.

[12] See Case C-230/16 *Coty Germany GmbH v Parfümerie Akzente GmbH* EU:C:2017:941.

[13] See *Commission Staff Working Document Evaluation of the Vertical Block Exemption Regulation*, SWD(2020) 172 final, 8 September 2020.

[14] See: <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12636-Revision-of-the-Vertical-Block-Exemption-Regulation>.

[15] The European Green Deal is the EU plan to create a sustainable economy, and provides for an action plan to boost the efficient use of resources by moving to a clean, circular economy, and to restore biodiversity and cut pollution. See further: https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.

[16] For Commission regulations that establish block exemptions applicable to horizontal agreements among competitors, see, *e.g.*, *Commission Regulation (EU) No 1217/2010 of 14 December 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of research and development agreements*, OJ L 335, 18 December 2010, pp. 36-42; *Commission Regulation (EU) No 1218/2010 of 14 December 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to certain categories of specialisation agreements*, OJ L 335, 18 December 2010, pp. 43-47; and *Commission Regulation (EU) No 316/2014 of 21 March 2014 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of technology transfer agreements*, OJ L 93, 28 March 2014, pp. 17-23.

[17] The *Vertical Guidelines* currently find that combined selective and exclusive distribution can only be block exempted if active selling in other territories is not restricted (para. 152). This dilutes significantly the impact that exclusivities are meant to have in a distribution network. The *Vertical Guidelines* currently only foresee the possibility of restricting active sales by selective retailers into other territories for the purpose of overcoming free-riding problems pursuant to an individual assessment (para. 63).

[18] As indicated above, qualitative criteria that are “overall equivalent” to criteria imposed on physical stores may also be imposed on Internet stores. Suppliers may also request that distributors have one or more brick-and-mortar shops or showrooms as a condition for becoming a member of its distribution system (*Vertical Guidelines*, para. 54).

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[19] See *Vertical Guidelines*, paras. 52-56. The Commission foresees very specific exceptional scenarios where dual distribution may benefit from an individual exemption under Article 101(3) *TFEU* (see para. 64).

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