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New EU Competition Rules for Purchase and Distribution agreements

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Background to the Commission's review of its policy on vertical restraints

- What are vertical agreements/vertical restraints and what are the competition issues associated with vertical agreements ?

- Positive past experience of Block Exemption Regulation (BER) and Guidelines (GL) :
  - Strong support to keep 1999 framework which introduced **effects-based approach**
  - Principle of **market share threshold** well accepted
  - **Meaningful enforcement** = relevant issues of foreclosure and softening of competition (collusion) + taking account of efficiencies
  - Since 2004: satisfactory interaction Commission-NCAs after modernisation of competition enforcement in EU. BER/GL ensure **consistent application**

- Objective of review last year : to update/improve 1999 BER and GL

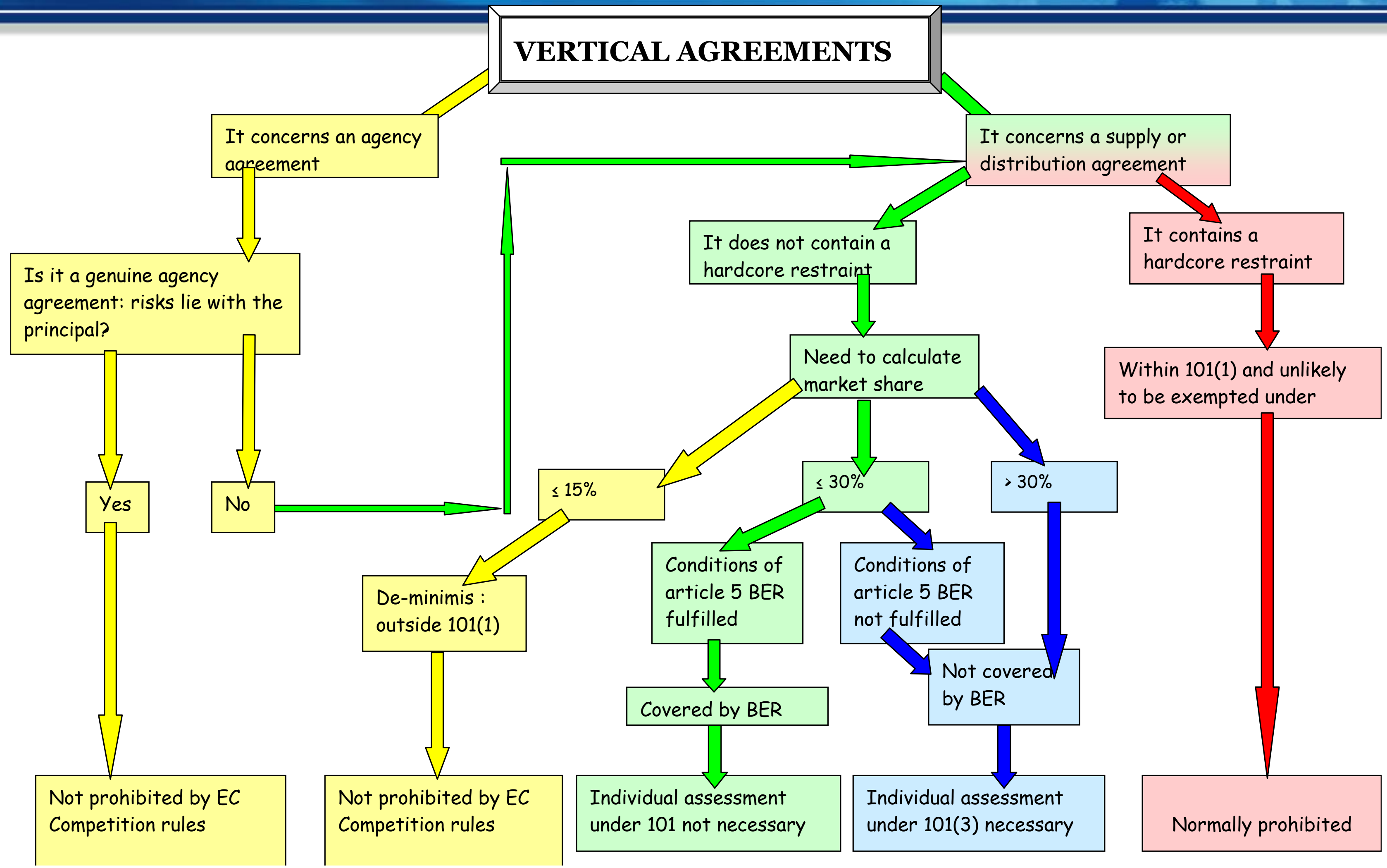
  Result of review: Commission adopts BER 330/2010 (OJ L 102 of 23.4.2010) and GL (OJ C 130 of 19.05.2010)

  Comp website: http://ec.europa.eu/competition/antitrust/legislation/vertical.html

Background: effects based approach

This effects based approach means:

- (a) Authority/plaintiff must show likely negative effects under Article 101(1) EC
- (b) Defendant must show likely efficiencies under Article 101(3) EC once likely negative effects are established (“consumer welfare test”)
- (c) “Safe harbour” as long as market share does not exceed 30% = block exemption => net positive balance presumed
- (d) Guidelines provide interpretation of the BER + guidance on a case by case assessment of negative and positive effects where the BER does not apply (above 30% MS)


VERTICAL AGREEMENTS
It concerns an agency agreement
It concerns a supply or distribution agreement
Is it a genuine agency agreement: risks lie with the principal?
Yes
No
It does not contain a hardcore restraint
It contains a hardcore restraint
Need to calculate market share
Within 101(1) and unlikely to be exempted under
≤ 15%
≤ 30%
> 30%
De-minimis : outside 101(1)
Conditions of article 5 BER fulfilled
Conditions of article 5 BER not fulfilled
Not covered by BER
Covered by BER
Not prohibited by EC Competition rules
Not prohibited by EC Competition rules
Individual assessment under 101 not necessary
Individual assessment under 101(3) necessary
Normally prohibited

Scope of the block exemption

Market share threshold: benefit of BER depends on both the supplier's and buyer's Market Share not > 30%

- Not only suppliers, but also distributors may have market power (e.g. supermarkets) => coverage by the BER should also depend on buyer's market share
- For supplier: share on the market where supplier <u>sells</u> contract products to the buyer
- For buyer: share on the market where buyer <u>purchases</u> the contract products from the supplier

Hardcore Restrictions (1)

- **To restrict at which price the buyer may sell (Resale Price Maintenance)**

  agreeing fixed or minimum resale price is a hardcore restriction, but not if recommended or maximum resale price

- **Sale restrictions: to restrict where or to whom the buyer may sell**
  - Passive sale restrictions are hardcore (main exception selective distribution)
  - Active sale restrictions are hardcore except to protect areas where there is exclusive distribution

Hardcore restrictions (2)

General clarification on the "hardcore approach"

- hardcore = no block exemption
  + presumption of negative effects under Article 101(1)
  + presumption it is unlikely that the conditions of Art 101(3) are fulfilled (§47)

- but individual exemption is not excluded in case of convincing evidence of likely efficiencies (§ 63-64 and 225)

- Hardcore approach = a "rule of reason" approach where the order of bringing forward evidence and showing effects is reversed

  - first likely efficiencies need to be shown by the firm
  - before the likely negative effects are shown by the authority

Hardcore restrictions (3)

Resale Price Maintenance (Guidelines §§ 219-225):

- **Possible negative effects:**
  - facilitation of collusion (both up- and down-stream), in particular if interlocking relations
  - elimination of intra-brand price competition: direct effect is price increase
  - loss of pressure on the supplier’s margin
  - loss of dynamism and innovation from in particular discounters

- **Possible positive effects:**
  - New entry: avoid free riding (efficiency already recognized for resale restrictions)
  - Support short term low price advertisement campaigns

Online Sale Restrictions (1)

<u>On the one hand</u>: Distributors should be free to have a website and engage in internet sales . . .

- Restrictions on the distributors' use of the internet are generally considered as hardcore restrictions of passive sales

<u>On the other hand</u>: Suppliers should be free to choose distributors/distribution format and prevent possible free riding between them

- **Exclusive distribution**:
  - Possibility to restrict active sales to protect exclusive distribution
  - Active selling: any efforts to be found specifically in a certain territory/by a certain customer group, e.g., unsolicited e-mails, targeted (online) advertisement (§ 53)
  - Cf. passive selling: having a website, responding to customer demand without soliciting them, different language options (§ 52)

Online Sale Restrictions (2)

<u>On the other hand</u> . . . (cont.) :

•To preserve quality of distribution and prevent free riding, GL clarify that the BER covers obligations to:

- have one or more “brick and mortar” shops (but not to punish successful online sales) (§ 54)
- impose a minimum amount of sales offline (also possible for the supplier to offer a fixed fee to support the distributor’s offline efforts) (§ 52(c))
- require quality and service conditions to be fulfilled for online sales that are overall equivalent to those applicable to offline sales (§ 56)
- use third party platforms only in accordance with standards and conditions agreed between the parties (§ 54)

<u>Conclusion</u> : new BER and GL do not impose or favour certain distribution formats but leave it to the consumers to “pick the winners”

More information on verticals:

http://ec.europa.eu/competition/antitrust/legislation/vertical.html