

The Commission Adopts New Vertical Restraints Block Exemption Regulation

On April 20, 2010, the European Commission published the revised block exemption regulation on vertical restraints (the “New BER”); the related guidelines on vertical restraints (the “New Guidelines”) will be published soon (together, the “New Rules”).¹ The New Rules will be applicable as of June 1, 2010, though with a transitional period for some agreements.² They will replace the previous block exemption regulation (the “Previous BER”),³ which expires on May 31, 2010, and the related guidelines (the “Previous Guidelines”) (together, the “Previous Rules”). The New Rules result from a long consultation process, concerning in particular the much-debated issue of the treatment of online sales.

The main change introduced by the New Rules is that, under the New BER, both the supplier and the buyer must meet the market share threshold of 30% for an agreement to be covered by the New BER and thus to benefit from an automatic exemption from the prohibition of restrictive agreements under Article 101 TFEU (the “Block Exemption”). Under the Previous BER, only the market share of the supplier was relevant.⁴

The New Guidelines offer much-needed clarification on the Commission’s approach to online sales within distribution agreements. They attempt to strike a balance between enabling consumers to benefit from distribution of goods and services via the Internet, while still allowing suppliers to regulate online sales. The distinction between active and passive sales, traditionally used to set the boundaries between “hardcore restrictions” and permissible restrictions, has been refined in the New Guidelines to

¹ Regulation 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, OJ 2010 L 102; the Guidelines were adopted “in principle” but the final text is to be published in May.

² Article 9 of the New BER provides that agreements complying with the Previous BER but not with the New BER will be exempted until May 31, 2011.

³ Regulation 2790/1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, OJ 1999 L336/21.

⁴ In the case of vertical agreements containing exclusive supply obligations, only the buyer’s market share was relevant, under the Previous BER (Article 2(2)).

specifically address online sales. “Active sales” include direct mail and targeted advertising such as ads directed at a particular territory or group of customers.⁵ “Passive sales” include non-targeted advertising, answering unsolicited requests by customers, or having a website (even if the website offers various language options). It follows that in most cases, the online activity of a distributor selling through its website will be considered “passive” selling that a supplier is generally not permitted to restrict.

The New Rules also make a number of changes and other clarifications regarding hardcore restrictions, which will be discussed in more detail below. Regarding exclusive distribution systems,⁶ the New Guidelines modify the notion of exclusive territory and customer group. A territory or customer group will be considered exclusively allocated even if the supplier is also actively selling products in that territory or to that customer group. With regard to selective distribution systems,⁷ the New BER provides that the supplier may restrict sales, both active and passive, by its resellers to unauthorised resellers in territories that the supplier reserved for itself but where it does not already sell products.

Finally, the Commission added two new sections, a section on upfront payments for access to a distribution system, and a section on category management agreements in the New Guidelines.

I. SCOPE AND STRUCTURE OF THE NEW RULES

The New Rules, like the Previous Rules, apply to vertical agreements, *i.e.*, agreements entered into between a supplier and a buyer.

Like the Previous BER, the New BER provides that a Block Exemption applies to agreements (i) where the market share threshold is met, and (ii) that do not contain hardcore restrictions. Agreements that are not covered by the Block Exemption must be assessed individually. In this regard, the New Guidelines are (like the Previous Guidelines) a helpful tool for companies to conduct a case-by-case assessment of the compatibility of distribution agreements with Article 101 TFEU.

⁵ See para. 53 of the New Guidelines.

⁶ Under exclusive distribution systems, the supplier undertakes to sell the contract goods or services only to a buyer that has been given exclusivity over a territory or a customer group. In addition, buyers undertake not to sell products actively on another territory or to another customer group that has been allocated exclusively to another buyer. See para. 51 of the New Guidelines.

⁷ In selective distribution systems, “the supplier undertakes to sell the contract goods or services [...] only to distributors selected on the basis of specified criteria.” In addition, the “distributors undertake not to sell such goods or services to unauthorised distributors within the territory reserved by the supplier to operate that system.” Article 1(e) of the New BER.

Finally, the New Guidelines expressly provide for the possibility to rebut the presumption that hardcore restrictions infringe Article 101 TFEU. To rebut the presumption, a company must show convincing evidence that (i) the agreement generates likely efficiencies and (ii) the agreement meets the other criteria of Article 101(3) TFEU. Although this flexibility is welcome, it is doubtful whether this clarification will have much effect in practice, as it will likely be difficult for companies to rebut the presumption.

II. MARKET SHARE THRESHOLD

As mentioned above, the New Rules reduce the scope of the New BER by introducing a narrower safe harbor. The 30% market share threshold now applies to both the supplier and the buyer.⁸ Regarding the supplier's share, the relevant market is the market in which the supplier sells contract products to the buyer. For the buyer's share, the relevant market is the purchasing market, *i.e.*, the market in which the buyer purchases the contract products from the supplier. This change reflects the increasing market power of large retailers.

III. HARDCORE RESTRICTIONS

As indicated above, the New Guidelines expressly provide that parties may rebut the presumption that hardcore restrictions infringe Article 101 TFEU. In addition, the New Guidelines specify that, within an exclusive distribution system, the supplier may be active in the same territory as an exclusive distributor. Moreover, the New BER provides that a supplier who sets up a selective distribution network may reserve territories for itself within selective distribution systems. Finally, although resale price maintenance ("RPM") remains a hardcore restriction, the Commission clarified its approach towards this practice, as further described below.

A. RE SALE RESTRICTIONS AS HARDCORE

The New BER does not substantially modify the list of resale restrictions that constitute hardcore restrictions. As a general rule, restrictions on passive sales remain hardcore, with some exceptions for selective distribution.⁹ Moreover, restrictions on active sales constitute hardcore restrictions unless they concern the operation of an exclusive distribution system.¹⁰ The first change brought by the New Guidelines is that restrictions on the buyer's place of establishment are no longer treated as hardcore restrictions.¹¹ In addition, although suppliers could restrict sales by wholesalers to end

⁸ Article 9 of the New BER.

⁹ Article 4 of the New BER.

¹⁰ Article 4 of the New BER.

¹¹ Article 4(b) of the New BER, to be compared to Article 4 of the Previous BER.

users under the Previous Rules, the New Rules provide that suppliers can also allow wholesalers to sell to certain end users in that territory (for instance to “*bigger end users, while not allowing sales to (all) other end users*”).¹² In addition, the New Rules make a number of changes concerning exclusive distribution and selective distribution.

Exclusive Distribution. The New Guidelines provide that a territory or customer group may be considered as exclusively allocated to the buyer even if the supplier sells products in the same territory or to the same group of customers; this was not the case under the Previous Guidelines. Thus, a prohibition of active sales in another distributor’s territory or to another distributor’s customer group does not constitute a hardcore restriction, even if the supplier itself sells products in that territory or to that customer group.¹³

Selective distribution. Under the New BER, a supplier can also restrict sales by its distributors to unauthorised distributors in territories that the supplier reserved for itself but where it does not yet sell products.¹⁴ In practice, suppliers who appoint selective distributors but reserve key countries to themselves on some territories were not covered under the Previous Rules. They would however be covered under the New Rules.

Hardcore restrictions outside Article 101 TFEU.¹⁵ The Commission also provides examples of situations in which otherwise hardcore restrictions fall outside of Article 101(1) TFEU or fulfill the conditions of Article 101(3) TFEU.¹⁶ For instance, a restriction of active sales to test a new product in a limited territory or customer group falls outside of the scope of Article 101(1) for the period necessary for testing.¹⁷ Moreover, the supplier’s restriction of active and passive sales to protect market entry for a new brand or a new geographic market falls outside of the scope of Article 101(1) for up to two years.¹⁸

¹² Para. 55 of the New Guidelines.

¹³ Para. 51 of the New Guidelines, to be compared to para. 50 of the Previous Guidelines.

¹⁴ Article 4(b)(iii) of the New BER, to be read in conjunction with para. 55 of the New Guidelines.

¹⁵ Paras. 60 to 64 of the New Guidelines.

¹⁶ Paras. 61 to 64 of the New Guidelines.

¹⁷ Para. 62 of the New Guidelines.

¹⁸ Para. 61 of the New Guidelines.

B. RESALE PRICE MAINTENANCE

In the New Guidelines, the Commission also clarifies its views on RPM.¹⁹ In principle, RPM remains a hardcore restriction giving rise to a presumption that such an agreement infringes Article 101 TFEU.²⁰ The New Guidelines provide additional details on the ways in which RPM may restrict competition, for instance by (i) facilitating collusion, (ii) eliminating intra-brand price competition, and (iii) reducing pressure on the supplier's margin.²¹

RPM may, however, also lead to positive effects, for example when (i) launching a new product, (ii) supporting short-term low-price advertisement campaigns or (iii) avoiding free-riding between distributors.²² These efficiencies will be assessed under Article 101(3) TFEU and weighed against the likely negative effects on competition. It will be for the parties to establish that the conditions for an exemption under Article 101(3) TFEU are met.

In practice, however, it is not clear how often the possibility to rebut the presumption that such practices infringe Article 101 TFEU will apply.

IV. ONLINE SALES

The New BER does not make any reference to online sales. The New Guidelines, however, deal with the issue at length and attempt to strike a balance between enabling consumers to benefit from the Internet while allowing suppliers to regulate online sales to prevent possible free-riding by certain distributors or distribution channels.²³

On the one hand, to ensure that distributors can operate a website and sell over the Internet, the following restrictions on passive selling constitute hardcore restrictions:²⁴

- Preventing distributors that operate a brick-and-mortar outlet from selling over the Internet;²⁵

¹⁹ Para. 224 of the New Guidelines.

²⁰ Article 4(a) of the New BER.

²¹ Para. 224 of the New Guidelines.

²² Para. 225 of the New Guidelines.

²³ See para. 107(1) of the New Guidelines for the notion of “free-riding”.

²⁴ Article 4(b) of the New BER and paras. 51 and 52 of the New Guidelines.

²⁵ Para. 52 of the New Guidelines.

- Requiring distributors to restrict access to the distributor website for customers outside of the distributor’s territory, or to refuse payments by cards that were not issued in the distributor’s territory;²⁶
- Limiting the proportion of sales distributors may make over the Internet;²⁷ and
- Requiring that products be sold on the Internet at a higher price than products sold in brick-and-mortar shops.²⁸

On the other hand, suppliers are entitled to (i) protect an exclusive distribution system by restricting active sales and (ii) regulate online sales in order to preserve the quality of the distribution network and prevent free-riding, in particular in the context of selective distribution. As a result, suppliers may:

- Prevent distributors from selling only through the Internet²⁹ and refuse to supply pure online players;³⁰
- Impose quality and service conditions, provided that these are equivalent to the conditions applicable to offline sales;³¹
- Require that a “*certain absolute amount*” of the products be sold through a brick-and-mortar shops and agree on a fixed fee with the distributor “*to support the latter’s online or offline effort*”;³² and
- Use third-party platforms only in accordance with standards and conditions agreed between the parties.

V. UPFRONT ACCESS PAYMENTS AND CATEGORY MANAGEMENT

In the New Guidelines, the Commission covers two new areas: upfront access payments and category management. The Guidelines discuss the possible anti-competitive and pro-competitive effects of each of these practices.

²⁶ Para. 52 of the New Guidelines.

²⁷ Idem.

²⁸ Idem.

²⁹ Idem.

³⁰ Para. 54 of the New Guidelines.

³¹ Paras. 54 and 56 of the New Guidelines.

³² Para. 52 of the New Guidelines.

Upfront access payments³³ may lead to anticompetitive foreclosure of (i) other distributors, if the payments “*induce the supplier to channel its products through only one or a limited number of distributors,*” and (ii) other suppliers, if the extensive use of those payments increases barriers to entry. Such provisions may also facilitate collusion among distributors. The Commission, however, recognises that possible efficiencies may arise, including “*efficient allocation on shelf space for new products*” and the reduction in “*asymmetry of information between suppliers and distributors.*”

Category management agreements do not usually raise competition law concerns.³⁴ Category management agreements may sometimes lead to anticompetitive foreclosure of other suppliers “*if the category captain is able to limit or disadvantage the distribution of products of competing suppliers.*” Such agreements may sometimes also facilitate collusion. The Commission, however, accepts that “*access to the supplier’s marketing expertise for a certain group of products*” may allow distributors to achieve pro-competitive economies of scale.³⁵

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³³ Upfront access payments are defined as “*fixed fees that suppliers pay to distributors in the framework of a vertical relationship at the beginning of a relevant period, in order to get access to their distribution network and remunerate services provided to the suppliers by the retailers.*” Para. 203 of the New Guidelines.

³⁴ Category management agreements are “*agreements by which, within a distribution agreement, the distributor entrusts the supplier (the “category captain”) with the marketing of a category of products including in general not only the supplier’s products, but also the products of competitors.*” Para. 209 of the New Guidelines.

³⁵ Para. 213 of the New Guidelines.

BRUSSELS

Rue de la Loi 57
1040 Brussels, Belgium
32 2 287 2000
32 2 231 1661 Fax

NEW YORK

One Liberty Plaza
New York, NY 10006-1470
1 212 225 2000
1 212 225 3999 Fax

WASHINGTON

2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
1 202 974 1500
1 202 974 1999 Fax

PARIS

12, rue de Tilsitt
75008 Paris, France
33 1 40 74 68 00
33 1 40 74 68 88 Fax

LONDON

City Place House
55 Basinghall Street
London EC2V 5EH, England
44 20 7614 2200
44 20 7600 1698 Fax

MOSCOW

Cleary Gottlieb Steen & Hamilton LLP
CGS&H Limited Liability Company
Paveletskaya Square 2/3
Moscow, Russia 115054
7 495 660 8500
7 495 660 8505 Fax

FRANKFURT

Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
49 69 97103 0
49 69 97103 199 Fax

COLOGNE

Theodor-Heuss-Ring 9
50668 Cologne, Germany
49 221 80040 0
49 221 80040 199 Fax

ROME

Piazza di Spagna 15
00187 Rome, Italy
39 06 69 52 21
39 06 69 20 06 65 Fax

MILAN

Via San Paolo 7
20121 Milan, Italy
39 02 72 60 81
39 02 86 98 44 40 Fax

HONG KONG

Bank of China Tower
One Garden Road
Hong Kong
852 2521 4122
852 2845 9026 Fax

BEIJING

Twin Towers – West
12 B Jianguomen Wai Da Jie
Chaoyang District
Beijing 100022, China
86 10 5920 1000
86 10 5879 3902 Fax