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EU Distribution Rules Under Review

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At a Glance

The European Commission (EC) has published a draft revised Vertical Block Exemption Regulation (VBER) and Vertical Guidelines (the Guidelines) for public consultation. The draft revised VBER and Guidelines are an important milestone in the EC's current review of the rules concerning distribution agreements, with implications for the digital economy.

Key Points

- The draft revised VBER and Guidelines follow a comprehensive evaluation process that started in October 2018. These two documents consider all the evidence that has been gathered, including results from public consultations, as well as comments and discussions with stakeholders and National Competition Authorities (NCAs).
- The proposed changes focus mainly on reflecting the digital economy, including the growth of e-commerce and online platforms.
- The proposed changes are consistent with the three objectives of the review:
  - Readjusting the safe harbour (or exemptions) provided by the VBER to its intended scope as regards dual distribution, parity clauses, active sales restrictions, and certain indirect measures restricting online sales
  - Providing guidance on e-commerce and online platforms; in particular, the application of the VBER and the Guidelines to online sales and advertising will be clarified, and specific rules relating to the platform economy will be included
  - Simplifying the complex areas of the current rules and streamlining certain provisions perceived as particularly complex, notably by small and medium-sized enterprises (SMEs)

Background

The EC is currently reviewing its competition rules on vertical restraints. The rules give parties to vertical agreements (entered into between businesses operating at different levels of the production or distribution chain) increased certainty about the compatibility of their agreements with Article 101(1) of the Treaty on the Functioning of the European Union (TFEU) by creating a safe harbour. The EC is assessing whether the rules are still fit for purpose, especially in view of the emergence and development of e-commerce.

In October 2020, the EC published an Inception Impact Assessment of policy options for its review of the EU Vertical Block Exemption Regulation (VBER) and accompanying Vertical Guidelines for consultation (see Latham & Watkins' *Antitrust Client Briefing*). In December 2020, the EC published a more detailed Impact Assessment for public consultation. These documents have led to the publication of the draft revised VBER and Guidelines.

What is the VBER?

The VBER aims to give parties to vertical agreements (entered into between businesses operating at different levels of the production or distribution chain) increased certainty about the compatibility of their agreements with Article 101(1) under the TFEU by creating a safe harbour.

Vertical agreements containing no "hardcore restriction" (e.g., resale price maintenance or territorial and customer restrictions) can be presumed to benefit from an exemption if neither party's market share exceeds 30%.

Agreements not satisfying the VBER criteria may still be compatible with Article 101(1) TFEU, but such agreements require individual assessment.

The VBER is accompanied by a set of guidelines (Guidelines on Vertical Restraints) that are designed to help companies self-assess.

The VBER entered into force in 2010, and will expire on 31 May 2022.

Key changes in the draft revised VBER and Guidelines

Readjusting the safe harbour

A tougher stance on dual distribution

Dual distribution refers to the situation in which a supplier simultaneously distributes its goods or services through independent distributors, but also directly to its customers.

Dual distribution developed significantly notably with the growth of online sales, which has facilitated direct sales by suppliers, either through their own websites or through marketplaces.

Dual distribution is currently exempted under the VBER. However, such situation may give rise to horizontal concerns (i.e., the supplier directly competes with its distributors). As a result, the draft revised VBER takes a tougher stance in this respect — including through the following measures.

- The draft revised VBER excludes from exemption the scenarios in which dual distribution gives rise to horizontal concerns. To this end, it proposes removing the safe harbour for all instances in which the parties' aggregated market share in the retail market exceeds 10%.
- The draft revised VBER provides for an additional safe harbour in which the supplier and its distributors have an aggregated market share at retail level above 10%, but still do not:
  - Exceed 30% market share of the relevant market on which the supplier sells the contract goods or services
  - Have the distributor hold a market share that exceeds 30% of the relevant market on which it purchases the contract goods or services

  The exemption shall apply, except for any exchange of information between the parties, which has to be assessed under the rules applicable to horizontal agreements.

  In order to benefit from dual distribution scenarios, the vertical agreements should exclude any by object restrictions.
- The draft revised VBER excludes providers of online intermediation services from the benefit of the exemption when they sell goods or services in competition with undertakings to which they provide online intermediation services.

Stricter rules for parity clauses relating to indirect sales

Parity clauses (or most-favoured nation clauses) require an undertaking to offer the same or better conditions to either: a) its contract party as those offered on any other sales/marketing channel (e.g., other platforms) — known as "wide" parity clauses, or b) on the company's direct sales channel (e.g., own website(s)) — known as "narrow" parity clauses.

Such clauses are increasingly used across sectors, notably by online platforms.

Both categories of parity clauses benefit from the block exemption under the VBER. However, NCAs and courts have identified anti-competitive effects stemming from "wide" parity clauses, (*i.e.,* obligations that require parity with other indirect sales or marketing channels, such as other platforms or other online intermediation services).

The draft revised VBER removes the benefit of the block exemption for such parity requirement and adds them to the list of excluded restrictions from the block exemption. As a consequence, this type of parity obligation would have to be assessed under Article 101(1) TFEU and may benefit from the individual exemption provided in Article 101(3) TFEU.

Conversely, the draft revised VBER still exempts retail parity clauses relating to direct sales or marketing channels (so-called “narrow” parity clauses) provided that the platform concerned has a market share of less than 30%.

More flexibility relating to active sales restrictions

Under the current rules, active sales (in which the buyer actively approaches individual customers) can only be restricted in a limited number of situations.

Suppliers often consider the current rules to be complex and unclear preventing them from designing their distribution systems according to their business needs.

The draft revised VBER introduces the possibility of shared exclusivity, allowing a supplier to appoint more than one exclusive distributor in a particular territory or for a particular customer group. In order to avoid the fragmentation of the single market, the draft revised Guidelines clarify that the number of appointed distributors should be determined in proportion to the allocated territory or customer group in such a way as to secure a certain volume of business that preserves their investment efforts.

In order to enhance the protection of the investment incentives of exclusive distributors, suppliers in exclusive distribution systems will be able to oblige their buyers to pass on to their customers if the customer of the buyer has entered into a distribution agreement with the supplier or with a party that received distribution rights from the supplier.

Concerning selective distribution systems, the draft revised VBER reinforces their protection from sales by unauthorized distributors located within the selective distribution network.

Indirect measures restricting online sales (dual pricing and equivalence principle)

Dual pricing involves charging the same distributor a higher wholesale price for products intended to be sold online than for products to be sold offline. The equivalent principle imposes criteria for online sales that are not overall equivalent to the criteria imposed on brick-and-mortar shops).

The development of online sales contributed to the creation of a well-functioning sales channel. Thus, the draft revised VBER no longer qualifies dual pricing as a hardcore restriction. As a result, dual pricing is authorized in so far as it is intended to incentivise or reward an appropriate level of investments and relates to the costs incurred for each channel.

Concerning selective distribution systems, the draft revised VBER takes into account the fact that online sales and brick-and-mortar shops are inherently different in nature. As a result, the criteria imposed by suppliers in relation to both channels no longer have to be equivalent.

The exemption will only apply to dual pricing and to the lack of equivalence if they do not aim to restrict online sales.

Guidance on e-commerce and online platforms

The draft revised VBER and Guidelines include guiding principles for the assessment of online restrictions drawn from the case law of the Court of Justice of the EU, namely in Pierre Fabre and Coty.

The draft revised Guidelines provide clarification on hardcore restrictions with a clear threshold easing the assessment for businesses — in particular, when certain online behaviours amount to active or passive selling. Moreover, a restriction of the use of price comparison websites or a paid referencing in search engines constitutes a hardcore restriction.

The draft revised Guidelines also deal with restrictions of the use of online platforms and price comparison tools.

Moreover, the draft revised VBER and the Guidelines provide specific rules and guidance relating to the platform economy. The revised draft VBER includes a definition of online intermediation services provider as supplier. The application of the rules to online intermediation services providers is set out in the Guidelines. These changes are consistent with the Digital Markets Act (DMA).

In addition, the draft revised Vertical Guidelines incorporate the February 2021 Working Paper on distributors that also act as agents for certain products for the same supplier (see Latham & Watkins' *Antitrust Client Briefing*).

The draft revised VBER aims to ensure a more harmonized application of Article 101 TFEU to vertical agreements across the EU. This objective is to be achieved by incorporating in the VBER itself certain guiding principles (e.g., those applicable to online sales restrictions), as well as new rules, including, for example, those regarding the definition and qualification of online intermediation services providers as suppliers. Moreover, the draft revised Vertical Guidelines aim to strengthen the NCAs' ability to withdraw the benefit of the VBER in individual cases by providing guidance on the applicable conditions and procedure.

Reducing compliance costs for businesses by simplifying the current rules and streamlining the existing guidance

The draft revised VBER introduces new definitions to give better clarity to businesses (e.g., suppliers, exclusive distribution systems, active sales, passive sales, restrictions of active or passive sales), in particular to SMEs.

The draft revised VBER simplifies the provisions on territorial and customer restrictions. These restrictions have been replaced by three distinct sets of provisions clarifying the scope of the prohibition for each of the main distribution systems, including:

- Exclusive distribution
- Selective distribution
- Free distribution

Each of these distribution systems are further explained in the draft revised Guidelines, which provide detailed guidance on the list of hardcore restrictions and exceptions that apply depending on the distribution system operated by the supplier.

Finally, concerning resale price maintenance (RPM), the draft revised Guidelines combine the previously scattered guidance on RPM in one dedicated section. The guidance includes an assessment of the effects of RPM on competition — and in particular, price monitoring, which is increasingly used in e-commerce does not constitute RPM as such. Moreover, an online intermediation services provider is prohibited to impose a fixed or minimum sales price for the transaction that it facilitates.

Next steps

2021	Public consultation on draft revised VBER and Guidelines open until 17 September for stakeholder comments.
Q4/2021	Finalisation of the Impact Assessment and submission to the EC Regulatory Scrutiny Board.
31 May 2022	New rules entering into force.

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