Additional public consultation
on proposed guidance relating to information exchange in the context of dual distribution,
intended to be added to the Vertical Guidelines

Comments from the Association of Inhouse Competition Lawyers ('ICLA')

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ICLA is an informal association of in-house competition lawyers with currently nearly 500 members across the globe. The Association does not represent companies but is made up of individuals as experts in the area of competition law. This paper represents the position of ICLA and does not necessarily represent the views of all of its individual members.

ICLA welcomes the European Commission's decision to initiate an additional public consultation to seek stakeholder input on the draft new section dealing with information exchange in a dual distribution context, which is intended to be added to the Vertical Guidelines (hereinafter "Draft Guidance"). In particular, ICLA appreciates that the Commission has chosen to react to the feedback it received from multiple stakeholders, including ICLA[1], on the treatment of information exchange in dual distribution scenarios in the draft revised VBER and Guidelines published on 9 July 2021.

ICLA shares the view that the Draft Guidance is a significant improvement vis-à-vis the approach in the draft revised VBER and Guidelines. It will provide more legal certainty for businesses in Europe. However, ICLA submits that there are still several items that require further clarification and most specifically in relation to:

- the description of exempted information exchange (see section III); and
- on the back of a great number of real-life examples, the wording of paragraphs 13 and 14 (see section IV).

I. Impact of the Draft Guidance on the draft revised VBER dated 9 July 2021

The Commission explains that the Draft Guidance aims to address the stakeholder feedback it received on the approach towards information exchange in dual distribution scenarios in Art. 2(5) of the draft revised VBER. However, it is not entirely clear whether this means that the Commission has decided to refrain from introducing an additional 10% market share threshold, as proposed by ICLA in its earlier submission. While the wording in the last paragraph of the Introduction as well as

[1] ICLA response to public consultation on the draft revised Regulation on vertical agreements and vertical guidelines - Sept 2021, p. 5 et seq. (available at http://competitionlawyer.co.uk/ICLA/Documents.html).

in para. 10 of the Draft Guidance suggests that Art. 2(5) of the revised VBER will indeed not include a requirement not to exceed a combined market share of 10% on the retail market for information exchange to benefit from the safe harbour, this is not expressly stated in the document.

Furthermore, para. 7 and 8 of the Draft Guidance imply that the European Commission will amend the wording in Art. 2(4), point (a) and (b) of the draft revised VBER to clarify that Article 2(4) exempts dual distribution on all levels of trade, and not only on the retail level.[2] Provided this understanding is correct, ICLA highly appreciates the European Commission's openness to take into account stakeholder feedback, including from ICLA.

In this respect, ICLA respectfully requests the European Commission to clarify the precise wording it intends to implement in Art. 2(4) and (5) of the revised VBER.

It is also not clear whether the European Commission is intending to maintain Art.2(6) in the draft VBER published in July. ICLA would here like to refer to its previous submission and request that this draft article is deleted.

II. General observations on the pro-competitive nature of dual distribution

Throughout its contributions to the evaluation of the VBER and the Vertical Guidelines,[3] ICLA stressed the importance to recognise that vertical relationships are generally pro-competitive, including in a dual distribution scenario. They open up intra-brand and inter-brand competition, providing customers with a choice of suppliers, which are able to compete on price/quality. The updated VBER should stress the pro-competitiveness of vertical relationships also in dual distribution relationships, rather than establishing stringent rules on companies setting up their distribution system.

Moreover, it must be recognised that as the supplier owns the brand, designs the products and drives the brand image, competition between a supplier and its distributors is by definition of a different nature than competition between independent distributors. The relationship between a supplier and its distributor is primarily a vertical relationship. The fact that the supplier chooses to market its products or services in parallel via a direct sales channel does not make the relationship "more horizontal". The downstream "competitive relationship" is subsidiary to and is created by the vertical agreement.

Dual distribution is common in many industries. Neither a recent phenomenon, nor an "invention" of e-commerce, dual distribution has existed for many decades across business sectors: B2B, industrial, retail, etc. Where suppliers use several channels to reach markets, these are complementary more than anything. This "division of labour" between a supplier and its distributors is governed by the aim to maximize output and reach, reduce costs and serve (end-) customers as efficiently as possible in order to be as successful as possible against the inter-brand competition. For example, in a B2B relationship, a supplier may focus its limited direct sales resources to serve a limited number of large key accounts and leave serving the often hundreds or even thousands of small and medium sized enterprises to its (indirect) distributors. The large key accounts – such as

[2] ICLA notes, however, that para. 8 still refers to the "retail level" and not to the "downstream level".
[3] All submissions are available on ICLA's website at www.inhousecompetitionlawyers.com.

large companies or public end users – will typically expect to side-step the distribution chain in order to deal directly with the supplier, often with the intention to negotiate special purchasing conditions (taking into account that these customers will place orders for large deals). On the other hand, wholesale and retail distributors will – due to their logistical capabilities – typically be better positioned to serve the SME segment more efficiently and at significantly lower costs than the supplier would be able to do via direct sales. This is all efficiency enhancing and pro-competitive.

When it comes to information sharing in a vertical relationship, ICLA stressed that this is beneficial and necessary to enhance the efficiency of the distribution network, and serve customer needs better. It is widely accepted that an exchange of commercial information between operators at different levels of a vertical supply chain – i.e., between a supplier and its distributor(s) – is part of a normal business dialogue. It is also recognised that such a business dialogue is generally a source of economic efficiency. These beneficial effects are not impacted by a supplier's decision to engage in parallel in direct sales. It follows from this that such unilateral decision does not constitute a sufficient ground to treat information exchange between a supplier and its distributor in a dual distribution scenario in the same way as information exchange between competing suppliers.

The Commission has not really provided any explanation or detail on the horizontal concerns posed by dual distribution, namely the "false positives" it aims to exclude from the safe harbour in the revised VBER. In the same manner, the Expert Report[4] falls short of providing any further explanation on the underlying "theory of harm". In particular, ICLA notes that the cases discussed in the Expert Report (p. 12 et seq.) fail to shed light on the specific risks associated with information exchanges between a supplier and a distributor in a dual distribution scenario. The only relevant case appears to be "*Hugo Boss*" – a classical hub-and-spoke scenario that fell short of the VBER (and was addressed under the Horizontal Guidelines). As recognised by the Expert Report (p. 12), the three other cases (*Guess*, *Apple France* and *XOM*) do not expressly discuss anti-competitive concerns with regard to dual distribution. In addition, it should be noted that the summary of the *Apple France* decision is factually incorrect and incomplete. The French competition authority did not find that the information exchanged between the parties infringed Art. 101(1) TFEU, and no fine was imposed in this respect.[5] Contrary to the considerations in the Expert Report, the fact that the dual distribution background was ignored in these three cases could be taken as signals that each of the three competition authorities, including the Commission, considered any potential anti-competitive concerns potentially stemming from dual distribution of lesser importance.

On the other hand, the Expert Report recognises that the VBER grants certain restrictions of intra-brand competition between a supplier and its distributors the benefit of the safe harbour. For example, in an exclusive distribution system, a supplier can restrict active sales by its distributors into territories or to customer groups that the supplier has reserved exclusively for itself. Moreover, a supplier can commit not to sell actively and passively into territories or to customer groups that it exclusively allocated to its distributors, because such a restriction on the supplier is not a hardcore restriction within the meaning of Art. 4(b) VBER. In this respect, the authors of the Expert Report consider that "*in an exclusive distribution set-up in which the supplier lawfully restricts its activities*

[4] https://ec.europa.eu/competition-policy/system/files/2022-02/kd0122032enn_VBER_dual_distribution_1.pdf.
[5] See Décision 20-D-04 du 16 mars 2020, para. 620, available on the website of the Autorité de la concurrence, at https://www.autoritedelaconcurrence.fr/fr/decision/relative-des-pratiques-mises-en-oeuvre-dans-le-secteur-de-la-distribution-de-produits-de-0.

to specific key accounts and legally or factually refrains from any other activity on the relevant market" there is no meaningful competition between a supplier and its distributors and hence this scenario should not even be regarded as dual distribution. In this context, the Expert Report also notes that while the supplier (who controls the purchase price for its distributors) may always be in a position to undercut its distributors, it may have no incentive to undermine its distribution system but instead has every incentive to strengthen its distributors and support their sales efforts (p. 24). Furthermore, the Expert Report notes that "*[t]he supplier's policy not to engage in price competition with its distributors is an inherent element of vertical and dual distribution situations, to which the supplier could even commit contractually*" (p. 49).

ICLA notes that while these observations are correct, they are not limited to exclusive distribution scenarios, but apply equally to other distribution set-ups. As explained above, dual distribution is typically guided by a division of labour in which the different sales channels complement each other, even if the supplier has not formally established an exclusive distribution system (which many suppliers regard as impractical). The supplier has no economic incentive to undercut its distributors if it wants to benefit from additional reach and reduced logistical costs by opening up an indirect route to market. Even if the supplier would have such incentive and act on it, they will only incentivize the distributors to look for alternative suppliers. This is all within the normal economic process and competition.

III. General requirement for information exchange to benefit from the safe harbour

In light of the general observations above, ICLA maintains the view that the requirement outlined in paras. 9 and 10 of the Draft Guidance, according to which information exchange only benefits from the safe harbour if it is "*necessary to improve the production or distribution of the contract goods or services by the parties*" is too strict. As stated above, the European Commission has failed to provide a sufficient explanation why information exchange in a dual distribution scenario should be presumed anti-competitive. Therefore, ICLA fails to understand why businesses should consider whether their normal day-to-day supplier-buyer information exchanges will result in efficiencies. Requiring companies to engage in an efficiency defence logically presupposes that the information exchange is considered a violation of Article 101(1) TFEU in the first place. Again, ICLA struggles to see that this is indeed the case. Moreover, shifting the burden of proof on businesses will increase legal uncertainty and costs as it adds an open norm into the application of the VBER. It will ultimately lead to inefficient supply chains as businesses may be deterred from sharing information along the vertical supply chain at all.

In our view, paras. 9 and 10 of the Draft Guidance, as well as the future VBER itself need to acknowledge the pro-competitive nature of dual distribution. Furthermore, it needs to be recognised that competition between a supplier and its distributors is different in nature and of secondary importance. In an exclusive distribution set-up, there may be no competition at all. Even outside exclusive distribution, competition is often limited in the interest of maximizing efficiency, for example if suppliers choose to focus on large key accounts and leave it to their distributors to serve other customer segments.

Taking this into account, it should be sufficient for the safe harbour that an exchange of information is *directly related to the implementation or facilitation of the vertical relationship*. In light of this, ICLA suggests to amend the wording in Art. 2(5) of the draft revised VBER as follows:

> *The exchange of information between a supplier and buyer does not benefit from the exemption provided by Article 2(1) of the Regulation where the information exchange is not ~~necessary to improve the production or distribution of the contract goods or services by the parties~~ directly related to the implementation or facilitation of the vertical relationship*.

IV. Examples in paras. 13 and 14.

ICLA welcomes the Commission's approach to provide examples of information types that are generally considered as unproblematic in para. 13. Such a positive list improves legal certainty as it provides companies, their respective in-house counsel, and national competition authorities with a clear tool to identify generally permissible conduct. However, in order not to unduly shift the burden of proof on businesses, it should be clarified that the list provided in para. 13 is merely a non-exhaustive list of examples. Furthermore, given the generally pro-competitive nature of vertical information exchanges and the failure to clearly identify the concerns as well as the "false positives" which the Commission aims to exclude from the scope of the safe harbour, it should be clarified that information exchange between the parties to a vertical agreement can be presumed pro-competitive.

For this purpose, para. 13 should be amended as follows:

> *13) ~~The following is a non-exhaustive list of examples of information that, when~~ Generally, all types of information exchanged by the parties to a vertical agreement that fulfils the conditions of Article 2(4), point (a) or (b) of Regulation (EU) X can ~~generally~~ be considered to be ~~necessary to improve the production or distribution of the contract goods or services by the parties~~ directly related to the implementation or facilitation of the vertical relationship and can therefore benefit from the exemption provided by Article 2(1) of the Regulation. The following is a non-exhaustive list of examples of such information:*
>
> *(…)*

With regard to the "negative" examples listed in para. 14, it should be clarified that the list provided in para. 14 constitutes a narrow exception to the general rule, according to which information exchanges are presumed pro-competitive and therefore covered by the safe harbour. For this purpose, the wording should be changed as follows:

> *14) ~~Conversely~~ Exceptionally, the exchange of the following types of information is generally not ~~necessary to improve the production or distribution of the contract goods or services by the parties~~ directly related to the implementation or facilitation of the vertical relationship.*

As for the exceptions, ICLA does not understand the Commission's reasoning behind the general exclusion of customer-specific sales data from exempted information exchanges currently foreseen in para. 14(b) of the Draft Guidance. The European Commission has not explained the specific concerns it associates with the exchange of customer information in a dual distribution scenario

that have led it to conclude that these types of exchanges generally cannot benefit from the safe harbour. It remains unclear which "false positives" need to be excluded. The (current and revised) VBER allows for the restriction of competition for customers between a supplier and its buyers in a dual distribution set-up. As recognised in the Expert Report, a supplier can agree not to (actively and passively) sell to customer groups it has exclusively allocated to its buyers. Such a restriction is not considered a hardcore restriction within the meaning of Art. 4(b) VBER.

In light of this, the only potential "false positive" that ICLA can identify with regard to the exchange of customer-specific information concerns the risk that a supplier may use such information to restrict competition between its distributors outside an established exclusive distribution system. However, addressing this potential concern does not require the broad exemption that is currently foreseen in para. 14(b) Draft Guidance.

Moreover, the wording in para. 14(b) fails to recognise that there are many valid reasons that require a supplier and its distributor to exchange such information. The Commission's focus on three limited exceptions in which an exchange of customer-specific sales data is regarded as unproblematic ignores a vast set of examples that should not raise competition law concerns. This is particularly relevant in the B2B area and industrial sector as well as in multi-tiered supply chains (i.e., consisting of suppliers – wholesalers – resellers) in which close collaboration is often required to meet inter-brand competition and satisfy (end-)customer needs. In particular, ICLA would like to draw the Commission's attention to the following examples:

- **Technical marketing:** In the industrial sector, a manufacturer often has to support its dealers, e.g. in the technical marketing of its products. In the case of complex technical products in particular, a dealer cannot know all the product details of all the products it sells and communicate them to the customer. In these cases, dealers often rely on the manufacturer's expertise, including through joint customer visits. This makes the identification of the individual customers as well as an exchange concerning their (technical and commercial) needs absolutely necessary. This is the only way customers can receive the best possible advice, particularly to distinguish the offering from other manufacturers' products (inter-brand competition).

- **Special projects / special customer conditions:** In particular in the B2B area (i.e., end customers are enterprises, including public end users), end customers often have special requirements and expect resellers to offer special conditions. Resellers will typically need support from the manufacturer to meet these expectations (such as special conditions on warranty, delivery times, additional discounts on supplier list prices, etc.). In order to meet the intensive inter-brand competition, a manufacturer will often be willing to grant such additional support, provided it can evaluate the commercial attractiveness of the special project / customer request as it needs to ensure an efficient allocation of its resources to effectively compete with other suppliers. For this purpose, it is necessary to exchange non-aggregated information between the manufacturer and the reseller, such as the identity of the end customer, main parameters of the project (e.g., type of products or services and special conditions needed, including expected volume), customer expectations (e.g., requirements of the customer for special conditions), etc. Moreover, in a multi-tiered supply chain, a request for special conditions from a reseller will often be passed through

by a wholesale distributor to the manufacturer. In such a case, the information needs to be exchanged between all parties involved in the vertical supply chain.

- **Acquisition of new customers:** Similar to responding to requests for quotes for special projects/ special end-customer requests, resellers may require support from manufacturers to acquire new customers, particularly in cases of strong inter-brand competition.

- **Fulfilment contracts:** In para. 178 of the draft revised Guidelines, the European Commission clarified that "*[t]he fixing of the resale price in a vertical agreement between a supplier and a buyer that executes a prior agreement between the supplier and a specific end user (hereinafter 'fulfilment contract') does not constitute RPM where the end user has waived its right to choose the undertaking that should execute the agreement*." However, in order to execute a fulfilment contract, the supplier will need to share with the buyer the identity of the end user as well as the pre-agreed resale price. Moreover, in its previous submission, ICLA explained that fulfilment contracts may also exist in a multi-tiered supply chain.[6] In such cases, information on the identity of the customer and the pre-agreed pricing may need to be shared between a supplier and a wholesale distributor as well as between the latter and a reseller.

- **Support for end of life deals:** A supplier may support its distributors in selling off ageing stock, for example by sharing information on potential deal opportunities (i.e., professional end customers that may be interested in purchasing the products) as well as providing additional discounts to allow attractive pricing. This requires the exchange of individualised customer information.

- **Multi-tiered distribution networks in general:** In many distribution networks, wholesale distributors act as intermediaries between a manufacturer and its resellers. In such a set-up, the role of the wholesale distributor is often not limited to the pure downstream distribution of products procured from the supplier. Instead, the wholesale distributor may be contractually required to take on additional tasks that overall enhance the efficiency of the supply chain. For example, a wholesale distributor may support the manufacturer in monitoring and enforcing a selective distribution network. For this purpose, a manufacturer and a wholesale distributor may need to exchange information concerning the authorized resellers that allow the manufacturer to evaluate compliance with the selection criteria. This may include, inter alia, the volume and value of sales generated with individual authorized resellers from the sale of the supplier's products by the wholesale distributor. In addition, outside a selective distribution system, suppliers often implement so-called partner programmes. A common feature of such programmes is that resellers will be eligible to benefit from additional incentives and/or volume discounts if they qualify for a specific partner status (e.g., silver, gold, or platinum partner). A manufacturer will often rely on a wholesale distributor to collect information from the resellers to determine the partner status and to calculate benefits. For example, a supplier may require the wholesale distributor to share information on the volume of products sold to a specific reseller to calculate volume rebates for the reseller. The manufacturer may also rely on the wholesale

[6] ICLA response to public consultation on the draft revised Regulation on vertical agreements and vertical guidelines - Sept 2021, p. 11 et seq. (available at www.inhousecompetitionlawyers.com).

distributor to pass-through such volume rebates to the relevant resellers. This requires an exchange of customer specific information between the supplier and the wholesale distributor. Moreover, a manufacturer may offer resellers to participate in promotional activities (e.g., by making available additional discounts on the manufacture's list price). In such cases, a manufacturer and a wholesaler will need to exchange information concerning the individual resellers that choose to participate in the promotional activities.

These examples are in no way exhaustive and there may exist many more valid reasons for suppliers and buyers (including in a multi-tiered supply chain) to exchange customer-specific information. Restricting the permissible exchanges to the three scenarios currently listed in para. 14(b) risks to eliminate long established business practices, particularly in the B2B space and industrial sector which create significant inefficiencies along the supply chain. As it appears impossible to list all relevant exemptions, ICLA submits that para. 14(b) should be replaced with a narrow wording that is limited to exclude the only potential "false positive" that ICLA can identify with regard to the sharing of customer information, i.e., if it is used to restrict competition between a manufacturer's distributors absent an exclusive distribution agreement. For this purpose, the approach taken in para. 13 and 14 vis-à-vis the exchange of recommended and maximum resale pricing could be mirrored. The following wording could be added to paras. 13 and 14:

- Add a new example in Para. 13:

  (x) Customer-specific sales data, including non-aggregated information on the value and volume of sales per customer, or information that identifies individual customers, provided it is not used to restrict the buyer's ability to determine its customers or to allocate customers between buyers absent an exclusive distribution agreement.

- And correspondingly amend the wording in para. 14(b):

  (b) Customer-specific sales data, including non-aggregated information on the value and volume of sales per customer, or information that identifies individual customers, ~~unless in each case such information is necessary to enable the supplier or buyer to adapt the contract goods or services to the requirements of the customer or to provide guarantee or after-sales services or to allocate customers under an~~ if it is used to restrict the buyer's ability to determine its customers or to allocate customers between buyers absent an exclusive distribution agreement.

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