

**RESPONSE TO EUROPEAN COMMISSION'S PROPOSED GUIDANCE RELATING TO
INFORMATION EXCHANGE IN THE CONTEXT OF DUAL DISTRIBUTION, INTENDED TO BE
ADDED TO THE VERTICAL GUIDELINES**

1. INTRODUCTION AND SUMMARY

- 1.1 K&L Gates LLP welcomes this opportunity to comment on the European Commission's proposed draft guidance on information exchange in the context of dual distribution ("Proposed Guidance"). Please note these views are our own as a firm and do not necessarily represent the views of our clients.
- 1.2 The Proposed Guidance is of major practical significance to many of our clients, especially given that many of our branded goods clients engage in dual distribution today or are planning to introduce or expand their direct to consumer businesses (accelerated by the supply chain pressures imposed by the Covid-19 pandemic and other economic factors). Our feedback in this paper supplements our earlier submissions to the European Commission ("Commission") dated 20 November 2020, 26 March 2021 and 17 September 2021, submitted in the context of the Commission's review of Vertical Agreements Block Exemption Regulation ("VBER") and the Vertical Guidelines ("VGL").
- 1.3 We commend the Commission for the clear and advanced draft of the Proposed Guidance. We are grateful for the Commission's significant efforts to create a pragmatic legal framework that supports the fast-moving commercial realities and challenges faced by market participants today.
- 1.4 **In summary:**
- (a) We welcome the Proposed Guidance being included as part of the VGL rather than under or part of the future Horizontal Guidelines. This avoids a period of significant uncertainty pending the new Horizontal Guidelines, and is eminently more appropriate given that the 'centre of gravity' in most dual distribution scenarios is the vertical supply relationship.
 - (b) We greatly welcome the Commission's apparent removal of the proposed combined 10% market share threshold for exemption of information exchanges. This helpful change correctly recognises, firstly, the limited restrictive effects on competition resulting from most vertical discussions, and secondly, that information exchange in dual distribution can improve distribution and indeed be necessary for generating consumer efficiencies, as suggested in paragraph 10 of the Proposed Guidance. The removal further enhances clarity and certainty of application of the VBER rather than introducing unintended confusion.
 - (c) We further welcome the inclusion of specific practical examples of likely exempted and likely excluded information exchanges, which will assist parties in the practical application of the Proposed Guidance.
- 1.5 Our main comment is that the proposed test for exempted information exchanges in paragraph 10 of the Proposed Guidance ("*the information exchange is not necessary to improve the production or distribution of the contract goods or services by the parties*") could exclude legitimate vertical exchanges posing little or no competition law risk, require a detailed assessment in each instance (thus removing the certainty and

efficiency benefits of the VBER), and introduce unintended legal consequences in practice. These comments are further discussed in section 2 below.

1.6 Accordingly, we would support wording similar to that proposed in the Expert Report on the review of the VBER (“Expert Report”); namely to permit information exchanges that are directly related and proportionate to implement and/or facilitate the main exempted vertical agreement.

1.7 In addition, in sections 3 and 4 below we have included comments on certain specific categories of information listed as examples in paragraphs 13 and 14 of the Proposed Guidance.

2. PRODUCTION OR DISTRIBUTION EXCEPTION

2.1 As summarised above, we are concerned that the test in paragraph 10 of the Proposed Guidance could lead to numerous unintended consequences.

2.2 By only permitting information exchanges necessary to improve production or distribution, the Proposed Guidance creates a new legal necessity test that would be difficult for commercial parties to apply in practice and effectively introduces an Article 101(3) TFEU type test.

(a) Notwithstanding the examples provided in paragraphs 13 and 14 of the Proposed Guidance, parties engaged in dual distribution could in practice be required to undertake a cumbersome self-assessment in the case of each instance of information exchange or piece of information, to determine whether the exchange between the parties is in fact essential or indispensable to improving production or distribution. The self-assessment required would negate the very purpose of the block exemption which is to ensure efficiency and certainty and lower costs and administrative burdens for businesses. It could also significantly impede the usual course of legitimate (non-restrictive) supply discussions.

(b) It will not always be obvious or simple to determine whether an information exchange meets both elements of the above test. It is quite conceivable that a specific exchange might only be *beneficial*, *convenient* or merely *habitual* in the *overall* scheme of an efficient supply and distribution relationship, or deliver other efficiencies (e.g. brand enhancement or lower prices for customers as opposed to improved speed of logistics which directly concern the products’ distribution).

(c) The proposed test could inadvertently introduce other burdensome and complex legal elements, such as those applicable to other “necessity” tests under EU competition law (e.g. no less restrictive alternatives to achieving the improvement).

(d) Typically, many if not most vertical exchanges in a dual distribution scenario have little or no restrictive effects, so the above effects are in any event disproportionate to the competition risk.

2.3 We would therefore suggest replacing the test in paragraph 10 with language similar to that in the Expert Report, to permit information exchanges that are directly related and

proportionate to implement and/or facilitate the main exempted vertical agreement between the parties. Subsequent references to this test would also need to be updated accordingly throughout the guidance. This broader test is proportionate to the competition risks concerned and would be significantly easier for parties to apply in practice. It also appropriately and simply excludes restrictive horizontal exchanges.

3. EXAMPLES OF PERMISSIBLE AND NON-PERMISSIBLE INFORMATION EXCHANGES

- 3.1 The Commission's introduction of examples of exchanges that would be considered necessary to improve the production or distribution of the contract goods or services, depending on the distribution model (in particular exclusive distribution, franchising and selective distribution) is helpful. We also welcome the introduction of a "white list" of information exchanges considered non-problematic in the context of dual distribution and a "black list" of exchanges of information presumed to fall outside the scope of VBER.
- 3.2 We agree with the Commission's list of examples in paragraphs 13 and 14 and would only point out some additional scenarios that we consider should be included or taken into account.

Sufficiently broad scope of promotional campaigns

- 3.3 Paragraph 13(f) of the Proposed Guidance correctly includes "Information relating to the marketing of the contract goods or services, including ... information on promotional campaigns for the contract goods or services, without prejudice to point (e) of this paragraph or paragraph (14) below."
- 3.4 Paragraph 14(a) excludes "Information relating to the actual future prices at which the supplier or buyer will sell the contract goods or services downstream, unless the exchange of such information is necessary to organise a coordinated short-term low price campaign in accordance with the guidance provided in paragraph [X] of these guidelines..."
- 3.5 It should be noted that in addition to coordinated discounting campaigns run across a network (and typically initiated by the manufacturer), in our experience it is not uncommon for a single retailer to approach the supplier, indicating that it wishes to run a promotion and asking if the supplier can part or fully fund the discount. In this scenario, it would be legitimate for the supplier to have visibility over the retailer's proposed discounted end price to determine the level of its financial support; and of course the exchange supports the delivery of consumer efficiencies in terms of lower prices.

Customer details

- 3.6 Generally speaking, we agree with the exclusion of the customer-specific information detailed in paragraph 14(b) of the Proposed Guidance. However, the Guidance should also be sufficiently broad to take account of the following legitimate exchanges of identifying customer information:
- (a) In the context of a selective distribution system, the supplier needs to know the identity of indirect reseller customers. The inability to identify a buyer's reseller customers would undermine the supplier's ability (and legal obligation) to ensure

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that goods are only being sold to and by authorised retailers, and that those indirect authorised retailers are compliant with the selective distribution criteria.

- (b) It is increasingly common for suppliers to reward or compensate retailers for strong performance or added value investments (e.g. in enhanced customer services, better brand presentation, more shelf or website presence etc.). Where a supplier does not sell directly to a retailer, this may be structured as a fixed bonus or rebate sum which the supplier obliges its direct distributor to pass on to a specific named retailer. In these circumstances, the supplier would need to know the identity of its customer's retail customer, to verify the latter's added value eligibility for the support.

- 3.7 Customer identity information in the above examples is necessary to deliver the significant efficiencies for consumers and to manage these aspects of a legitimate distribution relationship. The Commission is therefore encouraged to, for example, amend paragraph 14(b) to include additional examples.

4. CONCLUSION

- 4.1 In conclusion, we would like to commend the Commission again for recognising the need for a revision of the guidance concerning information exchanges in the context of dual distribution. There are numerous helpful clarifications and revisions in the Proposed Guidance which we believe will support the enhancement of consumer and economic welfare in Europe, and which offer sufficient flexibility to accommodate developments in the coming decade. We are grateful for the Commission's efforts and we remain available to discuss these or any other issues, and to assist the Commission with any additional information or clarification it may require in the finalisation of the VBER and VGL.