Freshfields Bruckhaus Deringer

RESPONSE TO THE EUROPEAN COMMISSION'S CONSULTATION ON THE DRAFT REVISED VERTICAL BLOCK EXEMPTION REGULATION AND GUIDELINES ON VERTICAL RESTRAINTS

17 SEPTEMBER 2021

1. INTRODUCTION

1.1 Freshfields Bruckhaus Deringer LLP welcomes the opportunity to respond to the European Commission's public consultation on the draft revised Vertical block exemption regulation (***DVBER***) and Guidelines on vertical restraints (***DVGL***).

1.2 This response is based on our significant experience and expertise in advising on issues raised by vertical agreements of many types, and in particular complex agency, exclusive and selective distribution arrangements, including many involving e-commerce and use of online platforms.

1.3 It is submitted on behalf of the Firm and does not represent the views of any of the Firm's clients, which comprise a wide range of companies that are both distributors and manufacturers or suppliers of different sizes and scope of activities. Likewise, this response does not necessarily in all respects represent the personal views of every partner in the Firm.

1.4 Overall, we strongly welcome the maintenance of the existing legal framework of a block exemption and detailed guidelines, both for the legal certainty and cost-effective means of compliance they provide to businesses, and for their contribution to the consistent application of competition law throughout the EU. We also welcome the many important clarifications and elaborations in the DVGL on the interpretation of the DVBER, and also on the application of Article 101 of the Treaty on the Functioning of the European Union (***TFEU***) in situations falling outside the scope of the block exemption, especially in relation to the new business models found in e-commerce and digital markets. However, market definition is difficult in many online cases. Guidance would thus be welcome as to how the markets are to be defined and market shares are to be calculated in the online context, especially in relation to online intermediation service (***OIS***) providers and dual distribution structures.

1.5 Further, we believe that there are aspects of the proposals which should be either changed or clarified in order to best achieve the Commission's stated goals (of "*eliminat[ing] false positives and reduc[ing] false negatives*", and of simplifying and streamlining the rules for businesses), especially as some far reaching changes appear in these drafts for the first time in this long running consultation. Below we comment in more detail on selected aspects of the DVBER and DVGL dealing with:

- Dual distribution
- Providers of online intermediation services: agency

- Providers of online intermediation services: classification as "suppliers"
- Parity clauses
- Restraints in e-commerce

2. DUAL DISTRIBUTION

2.1 We support the retention in the DVBER of the exemption for certain dual distribution arrangements, as well as its extension to cover wholesaler/retailer and importer/distributor relationships. However, we have concerns about (i) the introduction of a 10% market share threshold in respect of information-sharing aspects of dual distribution arrangements and (ii) the exclusion from the exemption of dual distribution involving OIS providers. We would also want to emphasize that (iii) clear guidance on information exchange in the vertical context is essential.

10% market share threshold

2.2 We understand that the Commission has concerns about certain horizontal aspects of dual distribution and in particular information exchange. However, the introduction of the new 10% retail market share threshold in respect of information-sharing aspects of dual distribution agreements adds unnecessary complexity and significant practical difficulties to the rules. This is undesirable, not least as it is contrary to the Commission's stated objectives in this review, which include simplification and streamlining of the rules.

2.3 It is important to recognise that the exchange of certain information between a supplier or manufacturer and its distributors is necessary for the proper functioning of many vertical agreements. This is also the case in a dual distribution context. These types of information exchanges are often crucial in developing product and service innovations which benefit consumers. To render dual distribution situations subject to materially greater risk of enforcement simply due to competing activities at the retail level would unjustifiably undermine manufacturers and others who wish to supplement an existing third party distribution network with some direct-to-consumer sales as well.

2.4 The introduction of the envisaged additional market share threshold could lead those suppliers who are reliant on their independent distributors to decide not to take the risk of selling directly into markets where they have concerns that they – combined with their distributor – might exceed the 10% threshold, thereby unnecessarily depriving consumers of an additional sales channel. This effect may be exacerbated by the fact that undertakings often struggle to establish their retail market share, because of uncertainties about geographic and product market definition. Notably, many National Competition Authorities consider the geographic scope of retail markets involving physical outlets to be local, with many different approaches taken depending on the nature of the retail outlet. This approach gives rise to significantly greater difficulty in self-assessing market shares than the 30% market share thresholds (which will often be markets of national or broader scope). The addition of this retail-level

threshold could therefore have the effect of causing the large proportion of distribution arrangements which are national (or broader) to exceed the 10% threshold in some parts of individual Member States while satisfying it in others. This result seems likely to increase confusion and dramatically reduce the benefits of block exemption.

2.5 Further, we observe that while a 10% threshold is consistent with the general *de minimis* threshold applicable to horizontal cooperation agreements, it is inconsistent with the 15% threshold applied to commercialisation agreements between competitors under the Commission's current Horizontal Cooperation Guidelines.

2.6 Finally, if the 10% threshold is retained – which we advise against strongly – the flexibility provided by Article 7(d) in cases where the 30% threshold is temporarily exceeded should also be extended to cover scenarios where the 10% threshold is exceeded. We also strongly recommend that guidance is included about the types of information exchange that are unlikely to cause concerns in those distribution arrangements that fail to satisfy the 10% retail threshold but would otherwise qualify for protection under the DVBER (see further below).

Exclusion of hybrid OIS providers

2.7 The absolute exclusion of hybrid OIS providers (those that both provide intermediation services and also sell goods or services in competition with their users) from the benefit of block exemption is unnecessary, not least because it denies the benefit of the safe harbour even to smaller hybrid companies. It may be that this absolute exclusion is inspired by the equation of hybrid platforms with digital gatekeepers, the latter being a concept from the draft Digital Markets Act which has been carried over into the present proposals. While the Commission may take the view that large hybrid OIS providers should not benefit from the safe harbour of the block exemption, this is already achieved by the general 30% market share which is a general condition of application of the DVBER. There is no justification for categorically excluding and therefore disadvantaging smaller OIS providers.

Guidance on vertical information exchange

2.8 Clear and practical guidance on vertical information exchange, in particular in dual distribution scenarios is essential. With suppliers now frequently selling products online via their own websites, dual distribution is now a well-established and prevalent business model.

2.9 The approach to information exchange in any guidance should therefore recognise that a manufacturer or supplier is not prevented from having normal discussions about a vertical relationship with its distributors simply because it also competes at the downstream retail level.

2.10 The DVGL provide no guidance at all on these issues. We understand that this is because it is intended that this will be covered in the Commission's Horizontal Cooperation Guidelines, currently under review. However, it seems more appropriate that this be covered in the DVGL. In dual distribution the horizontal aspect is an ancillary concern in relation to a business structure which is

essentially vertical in nature: indeed this is the rationale for including some dual distribution arrangements within the safe harbour of the block exemption. So any information exchange should be treated as such, rather than as primarily a horizontal exchange and addressed in the DVGL. Further, there may be significant legal uncertainty if the new 10% threshold enters into force prior to any new horizontal guidance becoming available.

2.11 Guidance should clarify that certain information exchanges in the context of a dual distribution agreement are block exempted, or may be exempted under Article 101(3) TFEU, for example where the market share thresholds are not satisfied. It should also indicate whether, and if so when, certain exchanges of information are likely to be problematic and how any competition concerns can be addressed as a practical matter. For example, many manufacturers support retailers' promotional activity by agreeing additional discounts or other funding for retailers' promotional periods, often in the context of discussions about the retailers' calendar of activities. To suggest that this conduct – which involves advance disclosure to the manufacturer of information about a retailer's future promotional plans – might not benefit from the DVBER because the manufacturer has its own (probably limited) retail presence and the retailer has a market share of more than 10%, will add considerable uncertainty and legal risk to a basic aspect of normal vertical relationships that operates for the benefit of consumers.

2.12 The US case, *Fortiline*,[1] may provide a useful precedent in developing such guidance. In that case, the Federal Trade Commission's (***FTC***) consent order specified that the following types of communication were not violations of Section 5 of the FTC Act: (i) requests by a distributor to receive prices, rates, rebates or discounts comparable to those that a manufacturer gives to other distributors and contractors/end users; (ii) negotiations for becoming an exclusive or quasi-exclusive distributor; and (iii) negotiations with a manufacturer to distribute products to contractors/end users previously or potentially served by that manufacturer.

2.13 Guidance in the DVGL should also recognise that many manufacturers and marketplaces institute firewalls, clean teams and place limits on data access, and so it should not be presumed that information flows create competitive concerns. It could also indicate the Commission's view on the effectiveness of different types of such mechanisms.

Other

2.14 Finally, it would be helpful for the DVGL to provide for some flexibility by indicating that the exemption is still applicable to agreements if any competing relationship at manufacturing level between the parties is marginal or not relevant, for example, if the distributor has a *de minimis* manufacturing presence thereby not affecting the essentially vertical nature of the agreement in question.

[1] Docket No. C-4592: https://www.ftc.gov/enforcement/cases-proceedings/151-0000/fortiline-llc.

3. PROVIDERS OF ONLINE INTERMEDIATION SERVICES: AGENCY

3.1 The development of new and modernised guidance on the application of the vertical restraints legal framework to the new business models of the digital economy are an important and welcome aspect of the DVBER and DVGL. In particular, we commend the apparent intention of the DVBER and DVGL to exclude the application of RPM rules to suppliers' setting prices and other terms when selling their produces via online platforms, discussed further in Section 4 below. However, the proposals are unsatisfactory in their current form, given the exclusion of OIS providers from classification as "agents", covered in this Section 3.

3.2 We observe at the outset that although the review of the vertical rules was launched in 2018, this approach to OIS providers was only introduced very late in the Commission's review process (with the publication of the DVBER and DVGL in July 2021), denying stakeholders the opportunity for meaningful engagement and consultation. Given the very significant potential implications of this aspect of the proposals, which might require fundamental restructuring of some business models and reappraisal of competition law compliance, businesses should have been given more opportunity to engage with the Commission on this. Instead, given the approach adopted, urgent clarification and amendment is now required.

3.3 As to agency, the DVGL are welcome insofar as they continue to recognise that risk is the core factor in the identification of agency relationships which, for certain purposes, fall outside of the scope of Article 101 TFEU.

3.4 However, we question the assertion (DVGL, para 44) that OIS providers cannot constitute agents, because they are categorised as suppliers in Article 1(1)(d) DVBER. An agent generally supplies an intermediation service to the principal, and the existence of such a relationship does not absolutely preclude the existence of an agency in the downstream sales relationship. There is no reason for the assertion implying that the law has changed in this respect. The DVGL should therefore instead confirm that OIS providers can in certain circumstances be "genuine" agents. A case-by-case assessment is needed, and the DVGL should set out what the relevant factors are.

3.5 Below we discuss in more detail first the exclusion of OIS providers as genuine agents, and then their consequential treatment in situations in which they nevertheless are contractual agents with related commercial functions.

Exclusion of OIS providers from being agents

3.6 The Commission has the power to decide, for the purposes of defining the terms used in the VBER, that OIS providers are "suppliers". We discuss the implications of this decision in Section 4.

3.7 However, the Commission does not have the power to change the law on Article 101(1) TFEU through statements in the DVGL.[2] This means that outside the

[2] Nor could the Commission do this through the DVBER, as its remit under the empowering Regulation 19/65 extends only to interpreting Article 101(3) TFEU and not Article 101(1).

VBER – that is, when applying Article 101 TFEU on a case by case basis – the general law on Article 101 TFEU, and in particular EU Court jurisprudence, applies.[3] The statement in the DVGL para 44 that the DVBER establishes that OIS providers do not qualify as agents "for the purpose of applying Article 101(1)" is therefore legally incorrect.

3.8 Instead, the question whether OIS providers may qualify as agents for the purpose of applying Article 101(1) TFEU depends on the case law on Article 101 TFEU. ECJ jurisprudence suggests that any undertaking – and there is no reason to exclude OIS providers – can be an agent if it fulfils the relevant criteria. The assessment should therefore be carried out on a case-by-case basis, as indeed is called for by a number of NCAs.[4]

3.9 This would also be in line with the Commission's decision in *E-books* which confirmed the possibility of concluding "genuine" agency agreements in an online environment with major online intermediaries such as Apple and Amazon.[5]

3.10 Nor do the DVGL adequately explain why sellers cannot appoint OIS providers as their agents. The consideration that OIS providers are "suppliers" should not on its own be a valid distinguishing factor, because they supply online intermediation services just as traditional agents supply intermediation services, and in any case, as already mentioned, their qualification as "suppliers" applies only in the context of interpreting the DVBER.

3.11 Other justifications given in the DVGL (para 44) as to why OIS providers can never qualify as agents are unconvincing and, in any case, generally refer to issues of fact that should be considered on a case-by-case basis:

"*Providers of online intermediation services generally act as independent economic operators and not as part of the undertakings of the sellers to which they provide online intermediation services*"

- The fact that both entities are "separate undertakings" is compatible with the "selling and purchasing function" of the contract goods or services forming part of the principal's activities; this is consistent with the approach taken to date by the Commission and EU Courts.[6]

"*strong network effects and other features of the online platform economy can contribute to a significant imbalance in the size and bargaining power of the*

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[3] See, e.g., cases T-325/01 *Daimler Chrysler v Commission* EU:T:2005:322; C-217/05 *Confederación Espanola de Empresarios de Estaciones de Servicio v CEPSA* EU:C:2006:784; and C-279/06 *CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL* EU:C:2008:485.

[4] Evaluation of the Vertical Block Exemption Regulation, Commission Staff Working Document, 8 September 2020, p. 122.

[5] EC Memo, 13 December 2012, available at: https://ec.europa.eu/commission/presscorner/detail/en/MEMO_12_983.

[6] Case C-279/06 *CEPSA* (see fn 4) ("*[special rules for agents cover] only the obligations imposed on the intermediary concerning the sale of the goods to third parties on behalf of the principal*").

contract parties and result in a situation where the conditions of sale of the contract goods or services and the commercial strategy are determined by the provider of online intermediation services rather than the sellers of the goods or services that are intermediated"

- This statement, presented as justification for the exclusion, is inconsistent with the Commission's decision in *E-books* (2012), which confirmed the possibility of concluding "genuine" agency agreements in an online environment with major online intermediaries such as Apple and Amazon.[7]

"*providers of online intermediation services often serve a very large number of sellers in parallel, which prevent them from effectively forming part of any of the sellers' undertakings*"

- The current Guidelines on vertical restraints (para 13) provide that "*it is not material for the assessment whether the agent acts for one or several principals*"; which is in line with the most recent EU court case-law.[8] Those words do not appear in the DVGL but the law on Article 101(1) TFEU cannot be changed merely by deleting this statement.

"*Providers of online intermediation services typically make significant market-specific investments, for example in software, advertising and after-sales services, indicating that these undertakings bear significant financial or commercial risks associated with the contracts negotiated on behalf of the sellers using their online intermediation services*"

- The costs of designing and operating a website or software are equivalent to (and have the same legal significance as) more traditional businesses' investments in premises/personnel (i.e. the basic costs of operating any business) and do not compromise the agency relationship (see also DVGL, para 38).

- An online intermediary's expenditure on advertising and search engine optimisation to attract consumers to its platform, which the intermediary is not contractually obliged to incur, are not "market specific investments" that compromise the agency relationship.

- EU Court case law provides that investments or activities that an intermediary undertakes at its own cost/risk may compromise its status as an agent only where those investments are "specifically

[7] EC Memo, 13 December 2012.

[8] Case T-418/10 *voestalpine v Commission* ECLI:EU:T:2015:516 (the existence of an agency relationship must be assessed individually vis-à-vis each principal "*in respect of, and to the extent of, the activities entrusted to [the agent] by each of [the principals]*").

required" in order to act for a principal or "*to the extent that the principal requires the agent to undertake such activities*".[9]

3.12 Finally, we note that the DVGL (para 44) state that "in principle" online platforms cannot qualify as agents. The meaning of the qualification "in principle" is unclear, as it could indicate that there are exceptions to this rule, which reinforces the need for clarification in this important area.

4. PROVIDERS OF ONLINE INTERMEDIATION SERVICES: CLASSIFICATION AS "SUPPLIERS"

4.1 The DVBER and DGVL's unequivocal categorisation of OIS providers as suppliers—and not buyers—appears to exclude the application of the RPM hardcore restriction (Article 4(a) DVBER) to firms selling their products via online platforms. We welcome this modification of the vertical restraints legal framework. However, given the importance of this rule, we think it should be expressly spelled out in the DGVL, for example, in Section 6.1.1 (Resale price maintenance).

4.2 Like the current block exemption regulation, the DVBER treats RPM—i.e. the "*restriction of the buyer's ability to determine its sale price*"—as a hardcore restriction. By definition, RPM is a restriction that a supplier imposes on a buyer that resells the product. Recognising the difficulty of assigning firms active in the online platform economy to such well-defined buckets (the DVGL, para 60), the DVBER ultimately opts to categorise OIS providers as suppliers (Article 1(1)(d)). The DVGL (para 63) further clarifies that an OIS provider "*cannot qualify simultaneously as a buyer […] in relation to the transaction that it facilitates*". The OIS provider cannot circumvent its qualification as a supplier "*by becoming a party to the transaction it facilitates or stipulating contractually that it is a buyer of the goods or services supplied on the basis of such a transaction*". This categorisation of OIS providers appears sensible to us as it better reflects the economic reality.

4.3 Given that the DVBER does not consider OIS providers to be buyers in relation to the intermediated products, it stands to reason that when a supplier of an intermediated product sets a sale price on an online platform, it cannot be considered RPM within the meaning of Article 4(a) DVBER. Regardless of whether this consequence was originally intended or not, we think this is the correct way of treating suppliers' setting prices on its products when selling via online platforms.

4.4 Acknowledging this interpretation of the DVBER will go a long way towards providing firms active in the online platform economy with legal certainty, which is the general purpose of the block exemption regulation.

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[9] Case C-217/05 *CEEES* (see fn 4) (holding that an intermediary may compromise its status as an agent if it makes investments that are "*required to enable the [intermediary] to negotiate or conclude contracts with third parties*" or "*commits himself to investing in advertising campaigns*"); Case T-325/01 *DaimlerChrysler* (see fn 4) (holding that costs assumed by an agent that "*is authorised, without, however, being obliged*" to promote sales at its own cost do not compromise the agency relationship).

5. PARITY CLAUSES

5.1 We welcome the new and much-needed increase in clarity now provided on parity clauses, particularly as the current divergence in approach between Member States on this issue has created significant legal uncertainty and complexity for businesses active across the EU. The inclusion in Article 5 DVBER of "wide" retail parity clauses, and the recognition in the DVGL of the complexity of the issues raised and the diversity of situations that may arise, with not all parity clauses being equivalent to restrictions imposed by online platforms, will contribute significantly to legal certainty in this area.

5.2 Parity clauses have become more common in e-commerce and offer scope for efficiencies (e.g. encouraging distributors to concentrate their selling efforts on the suppliers' products, facilitating customer investment or market entry and/or reducing transaction costs). At the same time, they can have anti-competitive effects (e.g. softening competition between retailers or platforms; impeding innovation; restricting expansion of small suppliers; facilitating collusion between retailers).

5.3 The structure for analysis set out in the DVGL for determining whether such clauses – to the extent that they do not benefit from the VBER – are likely to have anti-competitive effects and how any efficiencies resulting from the agreement in question can be weighed against identified restrictive effects under Article 101(3) TFEU is a positive development.

6. RESTRAINTS IN E-COMMERCE

Dual pricing and non-equivalence of selective distribution criteria

6.1 We support the proposal in the DVGL that dual pricing (different prices charged to a buyer depending on whether the product is to be resold online or offline) and non-equivalence as between online and offline selective distribution criteria, should no longer be treated as hardcore restrictions. This position is consistent with the case law of the EU Courts, in particular *Coty*,[10] and makes sense given that the current rules date from a time when online sales were less developed and were considered as needing protection, whereas now the converse is true and physical stores struggle to compete with online retailers – physical retailers now need protection from free-riding by online operators.

Restrictions on third party platform use

6.2 We similarly welcome the clarification in the DVGL, in line with *Coty*, that restrictions on the discernible use by a retailer of an unauthorised third-party online platform to make sales are not normally by object restrictions, and that limitations on the use of third party marketplaces are compatible with Article 101(1) TFEU where designed with, and proportionate to, the objective of preserving the luxury image and prestige of the goods and preventing the deterioration of their online presentation. The confirmation that this also applies

[10] Case C-230/16 *Coty Germany v Parfümerie Akzente* EU:C:2017:941.

to other products which are distributed on the basis of a legitimate selective distribution system is also helpful.

Use of online advertising and price comparison tools

6.3 We note the strict approach to limitations on online advertising, including price comparison tools, with restrictions that prevent the effective use of one or more online advertising channels by the buyers or their customers considered to be hardcore (DVGL, para 188). The same is true for restrictions on use of advertising on search engines, or an obligation on the distributor not to use the suppliers' trademarks or brand names for bidding to be referenced in search engines, or to provide price related information to price comparison tools.

6.4 We welcome the clarification in the DVGL that not all online advertising restrictions amount to hardcore restrictions under the DVBER, notably that (i) prohibition of use of – or other online advertising restrictions in relation to – "*one specific price comparison tool or search engine*" would typically not be regarded as preventing effective use of the internet because other comparison sites or search engines could be used to raise awareness (para 192(f)); and (ii) suppliers "*are allowed to give certain instructions to their distributors on how their products are to be sold*" irrespective of the distribution model applied (para 193). This guidance will be important for brand owners and providers of online advertising. But we would welcome additional clarification about how it will apply in circumstances where there is one very significant provider of online advertising services in light of the additional point made in the DVGL that restrictions on the use of "*all most widely used advertising services in the respective online advertising channel*" would nevertheless give rise to a concern.

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