Freshfields Bruckhaus Deringer

RESPONSE TO THE EUROPEAN COMMISSION'S CONSULTATION ON THE CURRENT REGIME FOR THE ASSESSMENT OF VERTICAL AGREEMENTS

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1. INTRODUCTION

1.1 Freshfields Bruckhaus Deringer LLP welcomes the opportunity to respond to the European Commission's public consultation on its current rules and policy on the assessment of vertical agreements, namely Commission Regulation 330/2010 on the application of Article 101(3) TFEU to categories of vertical agreements and concerted practices ("VBER"),[1] and the Commission Guidelines on Vertical Restraints ("Guidelines").[2]

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, and exclusive and selective distribution, arrangements. This response 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 suppliers of different sizes and scope of activities.

1.3 Likewise, this response does not necessarily in all respects represent the personal views of every partner in the firm.

2. EXECUTIVE SUMMARY

2.1 We are strongly in favour of 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 business, and for their contribution to a consistent application of competition law throughout the EU.

2.2 In particular we strongly support the retention of the VBER, but with the provision of some important clarifications and elaborations in the Guidelines on its interpretation, and also on the application of Article 101 in situations falling outside its scope, especially in relation to:

- platforms and digital markets, including issues relating to selective distribution;
- "most favoured nation" (MFN) provisions and other so-called "parity clauses";

[1] OJ 2010 L102/1.
[2] OJ 2010 C130/1.

- dual distribution, and in particular information sharing in this context;
- the concept and definition of "agent"; and
- resale price maintenance ("RPM").

3. GENERAL COMMENTS

3.1 Our experience of applying the VBER and Guidelines, although at times involving difficult issues of market share assessment and of application of the rules in the on-line environment, has been broadly positive. The legal certainty for business provided by block exemption under the VBER has frequently been helpful when advising clients on the competition rules. We believe, in addition, that the VBER and Guidelines have made a considerable contribution to the consistent application of Article 101 throughout the EU, whether by companies themselves or by national courts and national competition authorities ("NCAs"), although some updating of the Guidelines is now required to ensure that they can continue to play that role in future in the digital economy.

The benefit of the safe harbour

3.2 The current framework, and in particular the VBER, provides a safe harbour and therefore legal certainty for a great number of distribution agreements across the EU. There is also is now a very large number of agreements that have been drafted to conform so far as possible to the provisions of the VBER. Many businesses are thus able, with relatively little cost and effort, to assess whether their distribution arrangements are competition-law compliant and to engage in (re)negotiations with their business partners within a stable and relatively clear legal framework. The existence of the VBER, and the legal certainty it affords, also provides in-house lawyers and commercial negotiators with a valuable justification for conforming the provisions of their vertical agreements to the provisions of the VBER, including in circumstances where it might otherwise be more commercially advantageous to depart from those terms. We believe that this furthers the Commission's underlying policy objectives in promoting the positions set out in the VBER and Guidelines (e.g. limited duration of exclusivity provisions).

3.3 In the absence of the VBER assessment of agreements would be much more burdensome and therefore costly. Self-assessing vertical agreements can be difficult, as it involves determining whether there is a restrictive object, and if not, whether there are anti-competitive effects, and possibly whether the conditions of Article 101(3) are established. In addition, without the VBER, the commercial pressure to consider terms that are currently not within the its safe harbour, e.g. exclusivity provisions of a longer duration, would be likely be greater and there will be less obvious justification or benefit to continuing to observe the current limits.

3.4 The safe harbour provided by the VBER also frees up Commission and NCA resources. Since a large proportion of vertical agreements are, so far as possible, drafted in conformity with the VBER, resources can be concentrated on more serious competition law issues and on those vertical agreements that are likely to have the greatest negative effect on competition, either because of the nature of the parties to the agreements or of the restrictions contained within them.

3.5 For all these reasons we strongly support the maintenance of a block exemption and detailed guidelines and believe that this will also further the Commission's own objectives in encouraging and supporting a culture of compliance with competition law within the EEA without imposing undue burdens on undertakings.

Updating the Guidelines

3.6 Furthermore, while there is a need to look again at the current text of the Guidelines in order to make them as relevant as possible in relation to e-commerce and digital markets where there have been considerable developments since the time the Guidelines were originally written, we strongly encourage the Commission to maintain the VBER and Guidelines, with the level of clarity and relative ease of application that characterise the existing texts.

3.7 We also note that some of the greatest difficulties in advising on vertical restraints in practice arise out of diverging approaches as between the Commission and Member States' courts and authorities. This issue is becoming particularly acute in the area of e-commerce, for example in relation to online platform bans, "most favoured nation" clauses and other marketplace restrictions. These divergent approaches, often without any clear legal justification or basis, cause legal uncertainty for companies with a presence throughout Europe and risk fragmenting, rather than assisting the development of a single digital market. As a result of conflicting national decisions and approaches companies may have to, or choose to, adopt different business models in different EU Member States for their on-line distribution strategy.

3.8 Although the Guidelines have been an influential tool promoting consistency, it is now clear that, if they are to maintain their relevance in future, they require updating to allow account to be taken of new business models. In the absence of any such revisions we believe that the increasing tendency for national authorities and courts to adopt their own approaches to evolving issues in digital markets will increase in the coming years.

The distinction between "object" and "hardcore" restrictions should be clarified

3.9 We recognise that the Commission is requesting comments principally on the operation of the VBER (and clarification of its terms in the Guidelines). Because,

however, of the close link drawn by the Commission between "hardcore" restraints set out within the VBER and "object" restraints in its Guidelines we first comment on this issue of principle.

3.10 It is understood that the VBER operates as a safe harbour and that it should not exempt vertical agreements containing restraints, which might, in certain circumstances, entail a risk to competition. We believe, however, that the Guidelines should clarify that agreements which do not satisfy the VBER's conditions in each and every respect are not automatically assumed to restrict competition under Article 101(1) (to be restrictive of competition by object, see *Cartes Bancaires*[3]) or presumed not to benefit from Article 101(3) (see *GlaxoSmithKline*[4]), even if they may contain one or more "hardcore" restrictions.

3.11 We suggest therefore that it would be helpful for the Guidelines to include additional wording distinguishing the identification and treatment of restrictions "by object" (a concept which appears in Article 101 itself) and identification and treatment of "hardcore" restrictions (used in the VBER and Guidelines). Such clarification could conveniently be inserted into paragraph 47 of the Guidelines.

3.12 In particular, the Guidelines should clarify that the two concepts are not the same, and their crucial differences should be spelt out, i.e. that "hardcore" denotes restrictions specified in Article 4 of the VBER which preclude the VBER from applying and that "object" restrictions are those which are assumed, following an assessment of the agreement's content, objective and context, to have a restrictive purpose. Hardcore restraints are not necessarily restrictions of competition by object. Indeed, unlike hardcore restraints, object restraints cannot be specifically listed or defined. Paragraph 96 could also be reworded to make this distinction clear.

3.13 Clarification on this point, apart from being useful as an aid to understanding the Guidelines, could serve to diffuse certain criticisms of Commission policy that arise out of a misunderstanding of the implications of characterisation of a restriction as "hardcore".

4. VBER

4.1 We consider that the VBER should not be allowed to lapse, but should be renewed without significant modification. As currently drafted, it provides an important safe harbour for a vast number of vertical agreements which are most unlikely to create anti-competitive effects and which in many cases generate efficiencies in line with Article 101(3).

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[3] C-67/13 P, EU:C:2014:2204.
[4] Case T-168/01, EU:T:2006:265, *aff'd* Cases C-501, 513, 515, and 519/06, EU:C:2009:610.

4.2 We support the retention of Article 2(4) VBER which clarifies that certain dual distribution arrangements may be block exempted (and accepting that horizontal competitive concerns cannot be presumed simply from the fact that a manufacturer engages in dual distribution). Indeed, given that many manufacturers often sell products online via their own websites the prevalence of "dual distribution" has now become commonplace in the digital economy. In order to maintain their relevance, the VBER must acknowledge this new market reality and provide appropriate legal certainty and safe harbours in this context.

4.3 Further, we note that the level at which the market share thresholds are set is now well-established in the market and well understood by lawyers and business people (including those that are not experts in competition law). Given that they set the limits of a safe harbour the market share thresholds appear to allow a sufficient number of agreements to be brought within their scope without risking the possibility that agreements that may create competition issues are exempted. We have seen no evidence that supports a case to revise the current thresholds.

4.4 We do not support the expansion of the list of Article 4 hardcore restraints. For example, it should not be extended to cover any form of MFN provisions and other parity clauses. On the contrary, the different approaches that have been taken to these provisions at the national level illustrate the complex issues that these restraints raise, their scope for potentially pro-competitive effects, and the need for their careful appraisal and analysis under Article 101 (see further 5.13-5.14 below).

4.5 An approach that would be more useful to businesses and would avoid unintended consequences would be to further develop a coherent framework for the analysis of MFN/parity provisions in the Guidelines (see further section 5 below).

4.6 In addition to updating the Guidelines for MFN provisions, further guidance in the Guidelines clarifying the interpretation and working of a number of the other provisions of the VBER would however be helpful. For example:

(a) The meaning of "vertical agreement" and how the exception for non-reciprocal agreements between competitors at the buyer level applies could be clarified especially in relation to platforms (see further paragraph 5.7 below). For example, the Commission's Final report on the E-commerce sector[5] inquiry indicates that the "exchange of competitively sensitive data, such as on prices and sold quantities, between marketplaces and third party sellers or manufacturers with own shops and retailers may lead to competition concerns where the same players are in direct competition for the sale of certain products or services."[6] Given the vertical nature of such information

[5] 10.5.2017 COM(2017) 229 final

[6] Report from the Commission to the Council and the European Parliament: Final Report on the E-

exchanges, that the exchange of a certain amount of information is likely to be necessary to the proper functioning of many vertical agreements and that many manufacturers and marketplaces institute firewalls and place limits on data access it should not be presumed that these create competitive concerns in all circumstances. In addition, it would be helpful if the Commission could clarify that certain information exchanges in the context of a dual distribution agreement are covered by the VBER, and could incorporate further guidance on whether, and if so when, exchanges of information are likely to be problematic and how any competition concerns can be addressed as a practical matter.

(b) Market definition is difficult in many on-line cases. Further guidance would thus be welcome as to how the markets are to be defined and markets shares are to be calculated in the on-line context, especially in relation to platforms and dual distribution structures (see further paragraph 5.7 below).

(c) We consider that there is a need for further elaboration on the meaning in Articles 4(b) and (c) of both (i) "restrictions" on the territories into which, or the customers to whom, distributors can sell and (ii) "active" and "passive" sales. Specifically, clarification could be given on the circumstances in which, taking account of recent case-law of the EU Courts, the inclusion of the following terms or practices do and do not take distribution arrangements outside the scope of the VBER, especially in an on-line context:

- limitations imposed on distribution channels, both physical and on-line;
- limitations on use of price comparison websites;
- limitations on advertising (for example, using trade marks), search engine optimisation and search engine marketing restrictions;
- having a national domain in a country (co.uk or .de);
- location clauses;
- requirements to have a bricks and mortar store, including whether this may be required for each Member State in which the distributor wishes to sell; and
- dual pricing. The current guidelines indicate that dual pricing (where a distributor has to pay a higher price for products intended to be sold by the distributor online) constitutes a restriction of passive selling but accepts that in certain narrow circumstances dual pricing may fulfil the Article 101(3) criteria. In contrast, the e-commerce report recognises that dual pricing may be

Commerce Sector Inquiry (2017) at 14, para 56.

exempted, where indispensable to address free-riding. It would be helpful therefore if the guidance could clarify that dual pricing systems are frequently compatible with Article 101, especially in the context of selective distribution systems where brick-and-mortar dealers may have to invest significantly in their stores.

On all of these issues a realistic approach should be adopted in line with *Coty*;[7] so only the most stringent restraints on on-line selling (such as the de facto ban on selling imposed in *Pierre Fabre*[8]) should be treated as territorial sales restraints which prevent a distribution system (whether or not a selective distribution system) from benefiting from the VBER.

5. GUIDELINES

5.1 Overall the Guidelines provide a helpful level of legal certainty in respect of vertical restraints not falling within the scope of the VBER, but there are a number of areas in addition to those outlined in sections 3 and 4 above, especially in relation to e-commerce, where more clarity and/or additional guidance would be helpful. In particular and as already mentioned, it is vitally important that NCAs and national courts be given as much assistance as possible in applying the rules in as uniform a way as possible across the EU.

5.2 Amended or additional guidance would be helpful in the following areas:

- The concept and definition of "agent";
- The application of the rules to platforms and in digital markets, including their application to selective distribution;
- MFNs and other parity clauses; and
- RPM.

AGENCY

Platform sales

5.3 The guidelines and case-law are difficult to apply in many situations where sales are made on-line via a platform. The existing rules developed to deal with situations in which an agent operates as an "auxiliary organ" which forms an integral part of a principal's business, where their relationship is characterised by "economic unity". Although the principles have developed over time, greater guidance, perhaps

[7] Case C-230/16, EU:C:2017:941.
[8] Case C-439/09, EU:C:2011:649.

with worked examples, on how the agency principle applies to agency arrangements concluded between platforms and suppliers, and in digital markets, is needed. The current criteria are difficult to apply in this context (for example because it is now often the agent rather than the principal which adopts a policy with regard to commission levels) and provide significant scope for divergent approaches between different courts and EU competition agencies.

Fulfilment contracts

5.4 There are certain situations where, although the parties' clear intention is that there should be an agency relationship, and the arrangements are set up in that way, the agent takes on certain risks that do not fit with the standard interpretation of the agent/principal relationship.

5.5 Sometimes, for example, a third party facilitates "de facto direct sales" between a manufacturer and an end user, i.e. a manufacturer negotiates and agrees sales prices directly with an end user, and thereafter the third party is involved as an intermediary to purchase the products from the manufacturer and resell them to the end user, solely for the purpose of facilitating the distribution logistics, customer communication and collection of payment in return for commission. Despite the superficial appearance that the third party is "re-selling" the products at a fixed price, the anti-competitive concerns typically raised in relation to RPM do not apply, as the end user is able to negotiate directly with the manufacturer to achieve the lowest possible purchase price, and the third party would not have been able to achieve a better price as an intermediary.

5.6 This practice does not lead to any of the anti-competitive effects of RPM set out in para 224 of the Guidelines, and indeed creates efficiencies by ensuring the end user can obtain the lowest possible price. Bringing a facilitator/logistics provider into the distribution chain also helps the manufacturer to balance its commercial risks and break into a new or foreign market. Under the rule of reason approach applied to RPM in the United States, the pro-competitive benefits of such a structure would normally be expected to outweigh any potential anti-competitive effects. It would be helpful to have further clarification of how in practice the agency principle applies in these circumstances so as to give companies more guidance in self-assessing particular types of arrangements which may not fit neatly into the standard agent/distributor arrangements set out in the Guidelines.

PLATFORMS AND DISTRIBUTION IN THE DIGITAL WORLD

5.7 Given that the VBER and Guidelines were adopted at a time when e-commerce was less developed than today, there are various practical challenges in applying their concepts to distribution agreements with platform businesses. The Commission might therefore consider inserting a new section dealing specifically

with the application of the rules to platforms and dealing with issues that arise in relation to them, along with worked examples of how they apply to marketplaces/ platforms. This section could incorporate guidance on the following issues:

(a) When distribution arrangements with platforms may constitute agency agreements falling outside of the scope of Article 101 (see 5.3 above);

(b) When cooperation between a market participant retailer, which makes it platform/marketplace available to other sellers, constitutes a vertical agreement within the meaning of the VBER;

(c) How the rules on dual distribution apply in the digital world, where most businesses operate a dual distribution system or could easily do so, and in the light of this when firms operate as actual or potential competitors for the purposes of the VBER;

(d) How rules on information exchange apply in dual distribution situations and what steps firms should take to ensure that information exchanges are not treated as horizontal exchanges subject to more rigorous scrutiny under Article 101; this is of particular importance in the case of vertical exchange of data between marketplaces and third party sellers; and

(e) How relevant markets are to be defined and market shares calculated when applying the market share thresholds, especially where platform operators also act as retailers.

SELECTIVE DISTRIBUTION

5.8 Given the differences in treatment of selective distribution from other agreements under both the VBER, and Article 101(1) and their growing use as a means of distribution, it would be helpful to provide more extensive guidance on a number of issues relating to selective distribution.

Restrictions on marketplace sales for products other than luxury goods

5.9 In its *Coty* judgment, the Court of Justice held that clauses prohibiting authorised distributors from selling through third party marketplaces are compatible with Article 101(1) where designed with, and proportionate to, the objective of preserving the luxury image and prestige of the goods and preventing the deterioration of their on-line presentation. Such a prohibition "enables the supplier of luxury goods to check that the goods will be sold on-line in an environment that corresponds to the qualitative conditions that it has agreed with its authorised distributors". It also confirmed that such marketplace restrictions do not constitute hardcore restraints within the meaning of Article 4(b) and (c) of the VBER (they do not constitute a

restriction on the territory into which, or the customers to whom, authorised distributors could sell the luxury goods or a restriction on passive sales to end-users), irrespective of the type of product concerned, because the VBER does not limit its application to certain product categories.

5.10 In its application of Article 101(1), the Court specifically referred to restrictions applied for the distribution of luxury goods. Whereas the Court does not provide a definition of luxury goods, it refers to the "allure and prestigious image" and the "aura of luxury", that distinguishes luxury goods from other goods.

5.11 In the context of Article 101(1), it would be helpful if the Guidelines could clarify the extent to which the Commission considers that this aspect of the *Coty* judgment also applies to other products, which are distributed on the basis of a legitimate selective distribution system. The overall tenor of the Court's judgment suggests that the same conditions would also apply to other products, so long as the restraints are designed and proportionate, to the protection of the image of that product. Such a clarification is especially important given the divergent interpretations on this point being adopted by different national competition authorities. The French and Dutch competition authorities have followed the Commission's approach and upheld the legality of marketplace bans in relation to chainsaws and power tools and Nike's running shoes. Conversely, the German Federal Cartel Office ("FCO") considers that the application of the *Coty* judgment ought to be limited to luxury goods, for which a restrictive definition must be applied. The FCO has censored the use of market place restrictions in relation to Asics' running shoes and Adidas branded sports and leisure articles (even if *Coty* could be argued to allow this in the context of the application of the *Metro* criteria, the judgment does not give any such leeway in applying the VBER).

Non-discriminatory selection criteria for selective distribution contracts, freedom of contract and the duty to deal

5.12 Consistently with recent judgments issued by the Paris Court of Appeal, it would be helpful if the Guidelines could clarify that an individual decision not to accept a distributor into the selective distribution system does not either cause an infringement of Article 101(1) or remove the benefit of the VBER, so long as that decision does not form part of a general policy of the supplier to exclude one or more types of distributor from the selective distribution network.

MFNS AND OTHER PARITY CLAUSES

5.13 The Guidelines do not provide sufficient guidance on "most favoured nation" (MFN), price relationship agreements or contracts that reference rivals' prices (see also 4.4 above). They mention a "most-favoured-customer clause" as a potential means of strengthening RPM (para 48), and an "English clause" as a form of single

branding (para 129). Given that such clauses have become more common in e-commerce and offer scope for efficiencies (for example by encouraging distributors to concentrate their selling efforts on the suppliers' products, facilitating customer investment or market entry and/or reducing transaction costs), it would be helpful if the Guidelines set out a structured analysis for determining whether MFNs are in an individual case likely to have anti-competitive effects[9] and how any efficiencies resulting from the agreement in question can be weighed against identified restrictive effects under Article 101(3).

5.14 This is a particularly important area for attention, especially as these practices have, despite cooperation within the European Competition Network, been afforded divergent treatment by different NCAs (for example in relation to MFNs incorporated in contracts between hotels and online travel agents[10]) and provoked reactions from legislatures.[11]

RPM

5.15 The current guidelines seek to draw a compromise between an absolute prohibition of RPM and too generous acceptance of it. The former would fail to recognise that RPM, like other vertical restraints, may in some circumstances result in efficiencies, especially where necessary to launch new products, to penetrate a new market or to support a low price campaign within a franchising or selective distribution system, whereas the latter would go against the limited economic evidence available on the frequency and importance of any potential economic benefits flowing from RPM.

5.16 Even if it is not thought appropriate to remove such restraints from the list of hard-core restraints, and to create a rule of virtual per se legality for these practices where the VBER's market shares are satisfied, the current approach does not seem to have achieved the compromise sought – rather, given the enforcement practice (and risk of fines for incorporating RPM), the onerous requirements of Article 101(3) and lack of guidance on how they are to be applied, RPM is still considered by firms to be, essentially, illegal (firms do not have sufficient guidance as to, in particular, when these hardcore restraints are unlikely to create objective economic benefits, to benefit consumers, or to be indispensable to the attainment of any efficiencies created by the agreement). It would be helpful therefore if the Commission also indicated in the

[9] Given the relative lack of experience with these provisions and their potential to give rise to significant efficiencies, effects analysis should be conducted to ensure a fuller understanding of the clauses is accumulated.

[10] See e.g., the decision adopted in Germany 20 December 2013 (upheld on appeal), Report on the monitoring exercise carried out in the online hotel booking sector by EU competition authorities in 2016, http://ec.europa.eu/competition/ecn/hotel_monitoring_report_en.pdf and the decision of the Czech NCA fining Booking.com 8 million Czech Crowns, reported in MLex 18 December 2018

[11] See the Macron Law (France, August 2015).

Guidelines how in practice RPM efficiencies might be established (especially as the Article 101(3) Guidelines[12] provide limited guidance on how undertakings may provide evidence of non-price efficiencies), and also how they are to be weighed against the restrictive effects. This is especially important given that on-line RPM might be considered to be a crucial means of supporting the provision of dealer services in bricks and mortar stores and that RPM may be necessary to support the launch of new products for a few years or support occasional discounting campaigns. It seems crucial therefore that the Vertical Guidelines continue to recognize the potential pro-competitive benefits and to provide further guidance on how those benefits are to be reflected and given real and sufficient weight within the Article 101 framework. Without this, potentially pro-competitive arrangements may be deterred.

5.17 In addition the Commission could provide further guidance as to the limited circumstances, if any, in which recommended or maximum resale price maintenance constitutes a hardcore restraint. For example, in the e-commerce report the Commission suggests that the monitoring of online retail prices might "limit the incentives for retailers to deviate from [] pricing recommendations",[13] suggesting that the recommendation of resale prices when followed by monitoring might be treated as unlawful RPM. These types of concern may make firms unwilling to incorporate maximum and recommended resale prices in their agreements for fear that it could be misconstrued as RPM.

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[12] OJ 2004 C101/97.

[13] Report from the Commission to the Council and the European Parliament: Final Report on the E-Commerce Sector Inquiry (2017) (Final Report), 33.