Public questionnaire for the 2018 Evaluation of the Vertical Block Exemption Regulation

Response Annex

Question: *If you have rated one or several issues as "very low" or "slightly low", please explain the reasons for your rating. Please also explain whether the lack of legal certainty stems from (i) the definition of the particular area in the VBER or the related description in the VGL, (ii) their application in practice or (iii) the overall structure of the VBER and/or VGL*:

Response: There are 7 areas in which we believe that the VBER and VGL can provide better guidance and/or more legal certainty:

- ***Online sales restrictions***. We believe that the current sections regarding online sales in the VGL do not provide sufficient guidance in light of current market dynamics. Those dynamics have changed significantly since 2010. In particular, online sales have increased substantially over the last 10 years. Consumers have changed their buying habits as they purchase more and more online, and business strategies have evolved in order to meet the new and growing demand. Furthermore, there is an ever-growing offer of online market platforms, price comparison websites, online services etc. At the same time, markets have become increasingly digital, with the pace of innovation and 'change' being at the fastest speeds ever.

  Case law has evolved in response to some of those changing dynamics. The current guidelines do not take into account some of the above-mentioned changes and case law developments that have occurred since the entry into force of the current VBER. In particular, the VGL do not provide clarity regarding the ban on sales via third-party online market platforms in the context of selective distribution systems. In particular, there are no provisions relating to situations where authorized dealers resell products or services through online market platforms that are not authorized by the manufacturer, and/or do not fulfil the qualitative criteria that the manufacturer has specified in creating its selective distribution system. Further, courts across Member States have taken different views on this matter, leading to legal uncertainties and making pan-European advice more challenging.

  We therefore recommend that the VBER and VGL incorporate the latest case law as established in the CJEU *Coty* decision, and the guidance provided by the Commission in its Policy Brief published in April 2018. In particular, we recommend that the Commission includes the following principles:

  - Companies, which run selective distribution systems, are able to restrict their authorized dealers from reselling goods on third-party online market platforms as long as the companies' distribution model complies with the Metro criteria, i.e., that (1) the goods require a selective distribution system; (2) the company's resellers are appointed based on objective and qualitative criteria that are applied in a non-discriminatory fashion; and (3) the restrictions do not go beyond what is necessary;

  - The above-explained restrictions apply to any goods for which a selective distribution system can be justified, irrespective whether they are luxury goods, high-quality high-tech products, or any other type of products; and

- The restrictions should not be based on market share thresholds, i.e. any company running a selective distribution model irrespective of its market share should be able to benefit from the ability to impose the restriction on sales via unauthorized online platforms.

- ***Resale price maintenance***. Some Member States may have a stricter approach to RPM than others, which makes pan-European advice on the topic often challenging. The lack of global alignment brings additional complications. We therefore recommend that the Commission provides further clarity as to the circumstances in which RPM do not give rise to competition law concerns.

  In particular, in the VGL, the Commission recognizes that while RPM "*gives rise to the presumption that the agreement is unlikely to fulfil the conditions of Article 101(3) [...] undertakings have the possibility to plead an efficiency defence under Article 101(3)*" (para 223), and that RPM "*may also, in particular where it is supplier driven, lead to efficiencies*" (para 225). In practice, it has however proven to be challenging to convince the Commission of efficiency arguments (whether related to RPM or more broadly). The lack of legal clarity as to the circumstances in which the Commission may recognize that RPM brings sufficient efficiencies makes advising business clients more challenging.

  The Commission lists as a first example of situations in which RPM may bring efficiencies the introduction of new products, where "*RPM may be helpful during the introductory period of expanding demand to induce distributors to better take into account the manufacturer's interest to promote the product*" (para 225). We recommend that the Commission clarifies the conditions in which such efficiency defense is likely to be successful, as follows:

  - The duration for such introductory period should be at least 6 months, or possibly longer depending on the products or services in question;

  - There should be no limitations in terms of products' categories beyond the requirement that the products to which a promotion applies be new products;

  - Given the short period and the introductory stages of a product, there should be no need to provide detailed economic models to show the likely effects of the proposed RPM measures, or to prove that RPM will not have negative effects on intra-brand competition. It should be sufficient to rely on the manufacturer's intention to create favorable conditions for the successful launch of a new product, potentially by relying on contemporaneous strategy documents.

  The VGL further recognizes that RPM "*may be necessary to organise in a franchise system or similar distribution system applying a uniform distribution format a coordinated short term low price campaign*" (para 225). We recommend that the Commission clarifies which 'similar distribution systems' such efficiencies could apply to, as well as what the accepted reasons for RPM are in those situations. For example, we recommend that the Commission recognizes the efficiencies arising from manufacturers seeking to avoid that retailers free-ride on the extra demand that is being created by retailers who offer high-value services or invest into learning how to sell a new product, including through training or buying demonstration products or associated equipment. When limited in time, such pre-defined promotion campaign clearly benefits the end-user and only will have limited impact, if any, on intra-brand competition.

Finally, as far as the practice of *recommending* a resale price to a reseller or requiring the reseller to respect a *maximum* resale price is concerned, the VBER notes that such practices are only covered by the block exemption to the extent the market share of each of the parties to the agreement does not exceed the 30% (para 226). We do not consider that there are reasonable grounds to assume that the benefit of the block exemption should be limited in this regard, and recommend deleting the market share requirement – as long as, indeed, those practices are not accompanied by any price enforcement mechanisms or the use of maximum resale prices does not result in a *de facto* fixed resale price.

In this regard, we also note that the VGL adopts a narrow view when listing the market position of the supplier as the only important factor for the assessment of possible anti-competitive effects (para 228). A broader set of factors should be taken into account when assessing the effects of the practices in question, including the customer's buying power, relevant industry, product characteristics, timing, etc.

- ***Restrictions of cross supplies***. While we consider the VBER and VGL to be clear on the rules they intend to set out, we wish to point out that we rarely see cross-supply in practice. Adding additional resellers in the value chain will inevitably increase costs, which, in a highly competitive market and from a commercial perspective is not desired. Eventually, cost savings deriving from fewer resellers in the chain of distribution from a manufacturer to an end user result in lower prices to consumers. Other jurisdictions around the globe also take a much less stringent position on this point. We therefore would welcome the Commission considering to remove such restriction from the list of hard-core restrictions, and taking a more positive approach towards the efficiencies that can be achieved.

  As mentioned, purchasing a product or services from someone at the same level of trade will increase costs, as there are additional resale margins that need to be taken into account. Furthermore, while we appreciate that competition law seeks to serve the overall goal, *inter alia*, to avoid market allocation and promote the single market, it is not clear what goal the current restriction is seeking to serve. Restrictions of cross suppliers between members at the same level of trade would not prevent members of a selective distribution chain to purchase or sell to members based in other EEA states, or risk creating any market allocation concerns. For example, if a retailer in Greece would wish to benefit from cheaper products or services in Sweden, it would be free to purchase from a Swedish distributor. But it is highly unlikely that the Greek retailer would be able to benefit from better terms when purchasing from another retailer based in Sweden. Rather to the contrary, being able to streamline a supply chain will allow companies to increase cost efficiencies, and eventually allow to bring more beneficial pricing to the consumer of its products and services.

- ***Agreements preventing or restricting the sourcing of spare-parts***. The current VGL do not provide much clarity as to whether, within a selective distribution system, spare parts can only be purchased from authorized sources. In order to maintain the high-quality nature of the products that are subject to the selective distribution system, we strongly believe that a manufacturer should be able to limit the sourcing of spare parts to require purchases only through an authorized channel. Our experience has shown that allowing spare parts to be sourced outside the manufacturer's authorized channel can be highly detrimental to the quality and security of our products.

Like other technology hardware companies, our company faces widespread counterfeiting of spare parts. As an example, optical transceivers or modules that are plugged into a switch or router to provide high speed data transmission are an attractive target for counterfeiters. However, counterfeit spare parts may result in the entire switch or router not performing in accordance with its specifications. Further, counterfeit spare parts can introduce serious security vulnerabilities into the broader network as well as pose health and safety risks, including risk of electric shocks.

- ***Restrictions to sell brands of particular competing suppliers in a selective distribution system***. The VGL make broad statements in this regard, without investigating restrictions that, for example, only apply to a specific product or set of products of a given brand. More broadly, we consider that from the perspective of both businesses and the consumers to which they sell, there are good arguments to delete this restriction from the list of 'excluded restrictions', and/or recognize that there are circumstances in which such restrictions can create clear efficiencies. For example, there may be situations when the rationale for a restriction on the other brands an authorized reseller can sell may be justified by the need to encourage investments the supplier makes toward its authorized resellers or the need to protect sensitive commercial information the supplier provides to its authorized resellers.

  Manufacturers that adopt a selective distribution system may invest heavily into their resellers, by providing training, offering promotional materials or other types of support to ensure their resellers can efficiently market and sell their products and services. Other brands may not make such investments. This can lead to rivals free-riding on the investments made by a given manufacturer, disincentivizing such manufacturer from making further investments in the future, to the ultimate detriment of the consumer. In such cases, we believe there can be merit in seeking to allow suppliers in a selective distribution system to restrict the ability of their authorized resellers to sell products from particular competing suppliers.

  In addition, there may also be significant confidentiality concerns associated with the provision of certain software services. This is particularly important in situations, which often arise in the sale of technically sophisticated hardware and software products, that require close interaction between the supplier and its supply chain, and vice versa. For example, our company's specialized sales engineers frequently work closely with authorized resellers to design networks that address particular customer needs. A manufacturer deciding whether to undertake such close technical cooperation with an authorized reseller that also sells products from a direct competitor (which may be pursuing the same sales opportunity) may have a reasonable concern that information it provides to the reseller will be misappropriated for the benefit of its competitor. That concern may cause the manufacturer to limit its disclosure of information to the reseller, to the detriment of the reseller and the end customers it supports. Beyond exclusivity requirements, the manufacturer may choose to address those concerns by requiring that the reseller take reasonable measures to restrict the disclosure of information, which may include separation of physical sales locations, separate and isolated sales teams, and access controls in the reseller's IT infrastructure.

- ***Hardcore restrictions falling outside the scope of Article 101(1) of the Treaty or likely to fulfil the conditions of Article 101(3) of the Treaty***. Given the difficulty in bringing efficiency defenses, we recommend the Commission to provide examples or further clarity as to the

arguments companies would need bring in order to satisfy the conditions under Art. 101(3) TFEU.

- ***Exclusive supply***. The VBER and VGL would benefit from further clarity in terms of its alignment with the Commission's Guidance on its enforcement priorities in applying Article 102 TFEU to abusive exclusionary conduct by dominant undertakings, and in particular with the application of the as-efficient-competitor test.

Finally, we also wish to provide one further clarification regarding the market share thresholds. Especially in the fast-moving technology sector, market shares are not necessarily always an indicator of market power. Simply because a supplier and buyer have market shares above 30% does not necessarily mean that the restrictions they may apply will not lead to efficiencies. We appreciate that for suppliers and/or buyers in higher market share positions, an assessment is still required as to whether any potential efficiencies outweigh negative effects from a potential infringement of Art 101(1) TFEU. However, as per the Commission's enforcement practice as set out in decisions the Commission has issued applying Art 102 TFEU, the higher market shares should not necessarily cause a direct presumption that market power exists. As mentioned, a variety of factors should be taken into account when assessing market power, and this should not be different for any assessments in the scope of vertical arrangements. We appreciate that it may be challenging to build such factors into straightforward principles within the VBER. We do however consider it is important for the Commission to bear this in mind when confronted with specific cases.