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Expert report on the review of the Vertical Block Exemption Regulation

Final Report

Prepared by

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Competition

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Expert report on the review of the Vertical Block Exemption Regulation

Active sales restrictions in different distribution models and combinations of distribution models

Final report

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I. Executive Summary

This report contains the expert advice of Frank Wijckmans, prepared with the assistance of Sarah Jaques, on "*the use of active sales restrictions in different distribution models and combinations of such models*". It is part of the European Commission's Impact Assessment of the Review of the Vertical Block Exemption Regulation.

The expert advice reflects the business experience of the authors over the past 10 years with the application of the Vertical Block Exemption Regulation and the Vertical Guidelines. The authors illustrate their findings with (anonymized) business examples from their own practice, complemented with additional examples provided by specialized practitioners active in various Member States of the EEA.

The purpose of the report is to assess the impact of the different Policy Options identified by the European Commission in the Inception Impact Assessment as a result of the evaluation of the Vertical Block Exemption Regulation and the Vertical Guidelines.

The authors provide first a description of the most common distribution models encountered in actual business practice across the EEA. They then share their experience when considering the negative and positive effects of active sales restrictions which are stated in the Vertical Guidelines. They describe in a subsequent chapter the current regulatory framework and the key concepts relevant for the treatment of active sales restrictions under the Vertical Block Exemption Regulation and the Vertical Guidelines.

Prior to considering the impact of the different Policy Options both from a business and a consumer perspective, the authors map the difficulties and hurdles encountered in their practice with the current regulatory framework. The difficulties thus identified are important to appreciate the policy recommendations formulated in the subsequent chapters of the report.

The next chapter of the report provides a detailed assessment of the impact of the option not to implement any policy change (Policy Option I), the option to relax the current regulatory framework to offer suppliers more flexibility when designing a distribution system (Policy Option II) and the option to extend the exemption to sales restrictions from outside a territory in which selective distribution is operated (Policy Option III).

The authors conclude on the basis of their practical experience that it is not recommended to adopt Policy Option I. This will in their view imply that the possibility to use active sales restrictions remains in most cases no more than a theoretical possibility. Practitioners familiar with the current regime have steered away from active sales restrictions over the past years and Policy Option I is bound to continue and even increase such trend.

In respect of Policy Option II, the authors find that a certain degree of relaxation of the rules is necessary on some points and possibly advisable on other points. They distinguish between two key changes and other possible changes that may contribute to a more flexible and efficient approach adapted to the current and foreseeable business and market realities.

The two key changes relate to the abolition of the parallel imposition requirement (*i.e.*, the requirement for the supplier to impose a contractual obligation on all its buyers within the EEA not to engage in active sales restrictions in an exclusively allocated territory/towards an exclusively allocated customer group) and the relaxation of the rolling over prohibition (*i.e.*, the requirement that the restriction does not limit sales by the customers of the buyer). It is the opinion of the authors that,

without these key changes, practitioners will continue to steer away from the possibility of using active sales restrictions as a tool to address free riding or to instigate or protect investment by distributors.

Another area where the practical experience of the authors results in a recommended policy change is that of shared exclusivity. The report provides practical examples of cases where shared exclusivity matches better with the stated objectives or where formalistic compliance needs have caused the parties to implement single exclusivity scenarios.

The authors identify furthermore certain other areas where relaxation of the rules can usefully be considered (e.g., the complete abolition of the rolling over prohibition, customer-oriented channel management and the combination of exclusivity/selectivity at different trade levels). However, given the current regime, they lack practical experience with these specific areas and recommend that a further assessment is made by the European Commission before deciding on these policy options.

Finally, in respect of Policy Option III, the authors conclude that it makes eminent sense for the overall coherence of the regime to extend the block exemption of the selectivity requirement (*i.e.*, the prohibition on sales to unauthorized traders in territories where a selective distribution is applied) to all of the buyers of a given supplier and not just the buyers that are part of the selective network. The report provides concrete examples, particularly with regard to certain hybrid scenarios, where the current regime of the Vertical Block Exemption Regulation results in suboptimal solutions in this respect.

The overall recommendation of the report is to implement (i) the key changes referred to with regard to Policy Option II, (ii) shared exclusivity and (iii) the extension of the selectivity requirement stated in respect of Policy Option III. The report recommends a further assessment of the implications of the other changes mentioned in the context of Policy Option II. Finally, the report recommends more extensive and more readily accessible guidance in the future Vertical Guidelines with regard to the relevant issues so as to facilitate compliance and to reduce the cost of compliance.

II. Introduction

This report contains our expert advice for the European Commission's Impact Assessment of the Review of the Vertical Block Exemption Regulation (hereinafter "**VBER**" or "**Regulation 330/2010**") with particular focus on "*the use of active sales restrictions in different distribution models and combinations of such models*" (hereinafter the "**Report**").[1] It has been prepared by Frank Wijckmans (Professor at the Brussels School of Competition and Partner at the law firm **contrast**), with the assistance of Sarah Jaques (Counsel at the law firm **contrast**).

In order to collect a diverse range of examples from practice, the authors of the Report requested input from specialized practitioners in several Member States.[2] Their input has enabled us to draw on wider experience (both from a geographic and a sector perspective) when formulating our observations and recommendations.[3] In order to secure confidentiality, the Report presents examples from national practice anonymously and without reference to the Member State(s) to which the examples relate.

The Report also draws extensively on the experience of the Competition and EU law team of **contrast**. Examples and relevant questions and observations have similarly been anonymized to secure confidentiality.

The **first chapter** of the Report describes briefly the most common distribution models that are applied across the EEA. The objective is to go beyond the definitions contained in the VBER and the Vertical Guidelines and to identify the business applications of the various models that have been encountered in practice.

The **second chapter** of the Report summarizes the theories of harm and the positive effects (efficiencies) that are associated with active sales restrictions. It indicates the extent to which we have encountered these in practice and reflects certain observations that we heard formulated in our practice in respect of the relevant economic concepts.

The **third chapter** of the Report describes the current regulatory framework applicable to active sales restrictions. It touches briefly on scenarios where active sales restrictions may fall outside the prohibition of Article 101(1) TFEU, but focuses primarily on the current regime under the VBER and the Vertical Guidelines. It describes also briefly certain key concepts that are relevant for the assessment contained in later parts of the Report.

The **fourth chapter** of the Report attempts to map the difficulties encountered in practice with the implementation of the current regime. It is in this chapter that the input provided by the Contributing Practitioners will be relied upon mostly.

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[1] The information and views set out in this Report are those of the author and do not necessarily reflect the official opinion of the European Commission (hereinafter the "**Commission**"). The Commission does not guarantee the accuracy of the data included in this study. Neither the Commission nor any person acting on the Commission's behalf may be held responsible for the use which may be made of the information contained therein.

[2] We would like to thank the following law firms for their contribution: Eisenberger & Herzog (Austria), Delchev & Partners (Bulgaria), Divjak, Topić, Bahtijarević & Krka (Croatia), Havel & Partners (Czech Republic), Horten (Denmark), Arnecke Sibeth Dabelstein (Germany), Commeo (Germany), Pavia E Ansaldo (Italy), Banning (the Netherlands), Modzelewska & Paśnik (Poland), SRS Advocados (Portugal), Musat & Asociatii (Romania) and Cederquist (Sweden) (hereinafter the "**Contributing Practitioners**").

[3] The opinions expressed in this Report are those of the authors and they do not necessarily express the viewpoints of the Contributing Practitioners.

The **fifth chapter** of the Report addresses Policy Option I, notably the impact of implementing a policy of no change.

The **sixth chapter** of the Report addresses Policy Option II, notably the impact of relaxing the current framework to offer suppliers more flexibility when designing their distribution systems and the impact on consumer welfare.

The **seventh chapter** of the Report addresses Policy Option III, notably the impact of providing more protection of selective distribution systems by allowing restrictions on sales from outside the territory in which the selective distribution system is operated to unauthorized distributors inside that territory.

The **eighth chapter** of the Report contains our conclusions and recommendations.

III. Most common distribution models

In order to address the Policy Options meaningfully, it is important to have a clear understanding of the distribution models commonly used by the business in the EEA.

The authors of the Report find that it is common practice to work with non-exclusive and non-selective distribution. This is particularly so for smaller companies that, in their capacity of supplier, do not have the negotiation position to impose formalized distribution relationships or to administer distribution set-ups displaying a degree of complexity or sophistication. Our own experience, which is confirmed by the experience of the Contributing Practitioners, is that even larger companies often start out with non-exclusive and non-selective distribution systems. This may for example be the case when they enter new geographic markets or new product markets.

As will be discussed further in the Report, this observation has significant implications. It implies that, in the vast majority of cases, suppliers do not initiate their distribution set-ups within the EEA on the basis of an exclusive or selective model, but typically proceed from a less-formalized non-exclusive/non-selective format to a more sophisticated formula (exclusivity, selectivity, franchising) or a more formalized relationship. Transitions are therefore seldom made from a clean slate and must take account of legacies of the past.

Our experience shows that block exemption regulations have a considerable impact on the distribution formulas that are selected by the business and on the way in which they are devised. In our practice we have seen over time a considerable switch from exclusive distribution to selective distribution once Regulations 1983/83 and 1984/83 were replaced by Regulation 2790/99. This should not come as a surprise. The experience in the automotive sector, where already for decades both exclusive and selective distribution are block exempted, shows that certain sectors deem selective distribution more appropriate to meet their needs and, when offered the choice by the available block exemption regime, prefer selectivity over exclusivity. Hence, when reviewing the VBER, it is important to realize that compliance with the block exemption regime will in many instances be a more important driver of certain choices when setting up or modifying a distribution system than pure business logic or needs.

As regards exclusive distribution, our experience is that the request for such distribution model is often instigated by the distributor. A typical scenario is one where the relative strength of the parties sits with the distributor rather than the supplier. The distributor, who may have a strong reputation on the local market or who is prepared to develop a brand that is not yet well-known or requires further local development, seeks protection by means of its exclusive appointment. Conversely, the supplier may want to use exclusivity as an argument to persuade the distributor to take the new brand or products on board or to increase the focus of its activities on the supplier's products (e.g., by making special marketing or display efforts). It is important to record in this context that very often such an exclusive appointment is

sought or granted without necessarily accompanying it with protection against out-of-territory active selling. Any suggestion that exclusive distribution automatically goes hand in hand with active sales protection is in our experience false. As will be explained further in the Report, this is *inter alia* a consequence of the fact that practitioners (familiar with the stringent VBER requirements in this respect) will advise against relying on active sales restrictions.

Our practice shows that the reason why the distributor solicits exclusive distribution may be based on an incorrect understanding of the concept, which is often perceived to provide a degree of territorial protection that does not match with the block exemption reality. Reference can be made in this respect also to the difficulties to mount a system of protection against active sales in compliance with the VBER, the freedom enjoyed by the second tier players as a result of the rolling over prohibition and the treatment of internet sales under the VBER. Each of these points is addressed in more detail further in this Report. Once properly understood, quantitative selectivity (possibly linked with location clauses) is often considered to offer better protection against the free-riding concerns expressed by the distribution network.[4]

Exclusive distribution is applied in many different ways. We have seen cases where a distributor is in effect appointed as an exclusive importer covering an entire country, but also instances where the exclusive territory is defined with street names and local maps annexed to the distribution agreement.

Practice shows that exclusive distribution set-ups are not necessarily completely streamlined so that the exclusive appointment may be situated at different levels of the distribution chain. A typical scenario is one where a manufacturer/supplier operates with wholly-owned importers in its home or most successful markets and with independent importers in other markets. This implies that, in the former case, the exclusive distribution benefiting from the block exemption may sit one level down (typically retailer level) compared to the latter case (importer/wholesaler level). As will be seen further in the Report, this scenario triggers specific difficulties under the current block exemption regime (see, paragraphs 0-0 below).

In our experience, exclusive distribution is used in the vast majority of cases to provide territorial protection and not customer group protection. The concept of active sales protection for customer groups seems less well known by the business and their advisors. This is quite striking as in certain sectors customer segmentation may make eminent business sense.

As regards selective distribution, our experience is that it has become substantially more popular with the adoption of Regulation 2790/99, which stipulated for the first time the conditions under which selective distribution can benefit from a generally applicable block exemption regime.[5] This is partly also the result of the difficulties and

[4] Our practice seems to be confirmed by the finding in the evaluation study that "*distribution models which rely on territorial sales restrictions are becoming less viable. As a result, suppliers seems to be moving away from exclusive distribution models, at least at retail level, and shifting towards other distribution models such as selective distribution*". See, Commission Staff Working Document, *Evaluation of the Vertical Block Exemption Regulation*, SWD(2020) 172 final, 8 September 2020, available at https://ec.europa.eu/competition/consultations/2018_vber/staff_working_document.pdf (hereinafter the "**Commission Staff Working Document on the Evaluation of the VBER**"), page 38. See also, Commission Staff Working Document on the Evaluation of the VBER, page 189.

[5] Selective distribution was block exempted, prior to Regulation 2790/99, only for the automotive sector (Regulations 123/85 and 1475/95) and, for a certain period, also for franchising (Regulation 4087/88). The general block exemption regime applicable to vertical agreements covered only exclusive distribution (Regulation 1983/83) and non-exclusive distribution linked with an exclusive purchasing commitment (Regulation 1984/83).

legal uncertainties related to purely qualitative selective distribution (*Metro* conditions), which rendered this distribution formula unattractive prior to Regulation 2790/99. In our pre-Regulation 2790/99 practice, we have encountered business cases where legal certainty regarding selectivity was so important that businesses turned to franchising essentially for that reason (to be able to benefit from Regulation 4087/88). All of this shows the impact of a block exemption regime (or the absence thereof) on the decision-making pertaining to distribution systems. In our experience, the impact is not limited to the choice of distribution system, but extends to the clauses included in the relevant distribution agreements.

Certainly since the adoption of Regulation 330/2010 we notice that businesses are increasingly familiar with selective distribution. They now understand much better the difference between the conditions of the *Metro* scenario (purely qualitative selective distribution falling outside the scope of Article 101(1)) and the conditions to benefit from an exemption under the VBER. Experience teaches us that selective distribution is now applied on the basis of the VBER in many sectors which previously did not turn to this format. The ability to differentiate quality requirements between distributors has proven important to be able to roll out selective distribution throughout the EEA sufficiently simultaneously, as markets are not identical and, more importantly, the profile of the distributors that a given supplier is able to attract may differ from market to market. This may be the result of differences in the status of the supplier's brand or qualitative differences between the available distribution channels to which the supplier can turn.

When the switch to exclusive or selective distribution is made, our experience shows that businesses have difficulties to grasp the block exemption concepts. They are considered complex. Requirements that are familiar to the specialists are counterintuitive and not well-understood by business people. This is confirmed by the Contributing Practitioners and applies in particular to the current regime governing active sales restrictions (see also, paragraphs 0-0 below).

Franchising is applied in certain sectors and considered a separate format. The authors of the Report find that the business does not typically choose between exclusivity, selectivity and franchising. As the law stands, the choice for franchising is intentional and builds on the specific features of the distribution approach and needs. Where the business needs can be addressed sufficiently by selectivity, franchising will typically not be considered an equivalent alternative.

While it is a common belief that franchising at the retail level almost by definition includes a selectivity requirement – *i.e.*, no sales to unauthorized distributors – we find that this is not necessarily the case. For instance, in the food retail sector, it is not uncommon to operate franchising without a prohibition to sell to unauthorized resellers (*i.e.*, selectivity requirement). Given the nature of the products involved, this should not necessarily come as a surprise. In the food retail sector, there may not be such a need to restrict sales to a selective network of distributors and protection against active sales within an exclusive territory may in such a setting be deemed more relevant to protect a distributor's investments and sales efforts.

For purposes of this Report, it may suffice to add that the treatment of active sales restrictions in the context of franchising will depend on whether it is based on selectivity or exclusivity. For block exemption purposes, franchising will not steer an independent or separate course. If the franchise agreement meets the definition of selective distribution (Article 1(1)(e) of Regulation 330/2010), it must comply with the block exemption requirements for active sales restrictions applicable to selective distribution (see, Article 4(c) of Regulation 330/2010). In the opposite case, active sales restrictions included in a franchise agreement must meet the requirements of Article 4(b)(i) of Regulation 330/2010.

Agency is in our practice gaining increasing popularity. This applies also to the agency scenario where the agent does not assume more than *de minimis* financial and commercial risks. In this scenario, the imposition of an absolute territorial (or customer) ban does not present a problem as, in that respect, Article 101(1) TFEU does not enter into play. The position is different if the agent assumes relevant risks. If so, the agent is treated for block exemption purposes as a 'buyer' (see, the definition in Article 1(1)(h) of Regulation 330/2010).

In our experience, the business often perceives as counterintuitive the analogous treatment of the latter type of agents (sometimes called 'non-genuine agents') with independent distributors as regards territorial or customer restrictions. Although title transfers directly from the supplier to the customer, the supplier is sometimes uncertain whether it is legally entitled to reject orders presented by an agent who negotiated deals outside his area of responsibility (which might be defined in territorial or customer group terms or a combination of both). In our experience, it is exceptional that an active sales restriction is imposed in agency agreements and that such a restriction is imposed across the agency network. Principals may assume that this is not necessary in an agency set-up as they are the direct sellers to the customers. Due to the analogy with independent distributors, this assumption is not accurate. In our practice we have seen the last years increased awareness of this issue and, as a result, we have encountered over the past two-three years a marked increase in requests for advice on the conditions to qualify as genuine agents. Genuine agency allows the supplier (principal) to exercise more control over the field of activity of the agent (territory and customers), but also the pricing at which the agent negotiates on behalf of the principal.

When it comes to hybrid distribution models applied by the same supplier, the scenarios which we encounter most often are the following:

- A combination of exclusive or non-exclusive distribution for certain products with selective distribution for other products, implying identical geographies, but split product groups (sometimes, but not always within the same product market).

  For instance, a distinction is made by a supplier between premium products which are accompanied by a luxurious sales experience including extensive pre-sales and after-sales services for customers and other (non-premium) products for which such pre-sales and after-sales services are less relevant (see, e.g., the distribution set-up chosen by a supplier of kitchen equipment referred to in paragraph 0 below).

- A combination (even within the same geographic areas) of different selective distribution set-ups depending on the products involved, where different qualitative requirements are imposed and there is no complete overlap in terms of network members.

  For instance, a supplier's products are commonly distributed through a selective network, but the launch of a new high profile and more complex product offering is seized upon to reserve the distribution of such offering to a limited selection of the authorized distributors that is prepared to make additional investments in the launch and support of the new product. This results in a two-tier selective network. This approach is in our experience sometimes used to trigger a gradual increase in the qualitative standards applied by the network.

- A combination of distribution and agency set-ups,[6] sometimes for the same products but with differences in the customers that are targeted.

  For instance, a supplier distributes certain services through a non-exclusive distribution network and relies on some of the network members to act as agents for the sale of the services to larger accounts that wish to contract directly with the supplier.

We are aware that stakeholders refer to combinations of exclusivity in certain territories and selectivity in other territories, or exclusivity at the wholesale level and selectivity at the retail level. Clients occasionally raised these scenarios with us, but, once the constraints presented by the VBER were properly understood, they were in most cases abandoned (see, paragraphs 0-0 below). When confronted with questions in this respect, we tend to steer the business away from them given their intrinsic difficulties under the VBER. Hence, when we have encountered these hybrid formats, they were typically legacies of the past and not the reflection of a deliberate strategic choice. We address the difficulties pertaining to these hybrid models in more detail in chapter V (see, paragraphs 0-0 below).

IV. Theories of harm and efficiencies

This chapter summarizes the negative and positive effects of active sales restrictions from an economic perspective. It is based upon the effects identified in the Vertical Guidelines. As we are not economists, it is not the objective of this chapter of the Report to assess the economic theory related to active sales restrictions. We take the effects as described in the Vertical Guidelines as a given and match them with business cases and experience encountered in our advisory practice. We add certain observations formulated by stakeholders in the context of our practice that may be of assistance to the ongoing impact assessment.

A. Negative effects of active sales restrictions

The Vertical Guidelines (paragraph 151) identify the negative effects in respect of exclusive distribution as a whole and do not specifically address the negative effects of active sales restrictions. They provide that "*[i]n an exclusive distribution agreement the supplier agrees to sell its products to only one distributor for resale in a particular territory*" and add that the exclusive distributor "*is usually limited in its active selling into other (exclusively allocated) territories*" (emphasis added). We assume therefore that the negative effects listed for exclusive distribution are also relevant to identify possible negative effects of active sales restrictions linked to an exclusive distribution system.

The stated effects are the following. *First*, restrictions within exclusive distribution may have the effect of reducing intra-brand competition between distributors. *Secondly*, when the restrictions relate to where a buyer can sell, it may create market partitioning and facilitate price discrimination. *Thirdly*, when most or all of the suppliers apply exclusive distribution, this may soften inter-brand competition and facilitate collusion. *Fourthly*, exclusive distribution may result in foreclosure of other distributors (Vertical Guidelines, paragraph 151). The Vertical Guidelines (paragraph 101) specify more generally that negative effects that result from vertical restraints at the manufacturers' level "*may harm consumers in particular by increasing the wholesale prices of the products, limiting the choice of products, lowering their quality*

[6] This has also been addressed by the Commission in its Working Paper, *Distributors that also act as agents for certain products for the same supplier*, February 2021, available at https://ec.europa.eu/competition/consultations/2018_vber/working_paper_on_dual_role_agents.pdf.

or reducing the level of product innovation" and that negative effects at the distributors' level "*may harm consumers in particular by increasing the retail prices of the products, limiting the choice of price-service combinations and distribution formats, lowering the availability and quality of retail services and reducing the level of innovation of distributors*".

We encountered in our advisory practice a number of points that may be relevant when such possible negative effects are relied upon when determining and assessing the impact of the future block exemption regime:

1. Importance of online sales and the qualification as 'passive sales'

The Vertical Guidelines provide that the nature of the product is not particularly relevant to the assessment of the possible anti-competitive effects of exclusive distribution.[7] In our experience, this statement no longer appears to be accurate.

Anno 2021, the market reality is that certain types of products are very commonly bought online. Reference can be made in this respect to the Commission's support study on consumer purchasing behaviour in Europe.[8] In response to the question whether the last purchase made by the customer was made online or offline, it showed that 47% of the purchases of cosmetics and hair care products, 66% of clothing and shoes, 60% of house and garden equipment and 75% of consumer electronics and large electrical appliances were made online. The figures can be expected to have increased since the COVID-19 outbreak in Europe.

Under the current VBER regime, online sales are generally considered passive sales, which cannot be restricted in an exclusive distribution system.[9] The Vertical Guidelines describe under which circumstances internet sales qualify as active selling.[10] In view hereof, we interrogated the Contributing Practitioners very specifically on their

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[7] Vertical Guidelines, paragraph 163: "*The nature of the product is not particularly relevant to the assessment of possible anti-competitive effects of exclusive distribution. It is, however, relevant to an assessment of possible efficiencies, that is, after an appreciable anti-competitive effect is established*".

[8] Commission, *Support studies for the evaluation of the VBER – final report*, Publications Office of the European Union, 2020, available at https://op.europa.eu/en/publication-detail/-/publication/93f52e95-a92e-11ea-bb7a-01aa75ed71a1.

[9] Vertical Guidelines, paragraph 52: "*[…] In general, where a distributor uses a website to sell products that is considered a form of passive selling, since it is a reasonable way to allow customers to reach the distributor. The use of a website may have effects that extend beyond the distributor's own territory and customer group; however, such effects result from the technology allowing easy access from everywhere. If a customer visits the web site of a distributor and contacts the distributor and if such contact leads to a sale, including delivery, then that is considered passive selling. The same is true if a customer opts to be kept (automatically) informed by the distributor and it leads to a sale. Offering different language options on the website does not, of itself, change the passive character of such selling*".

[10] Vertical Guidelines, paragraph 53: "*A restriction on the use of the internet by distributors that are party to the agreement is compatible with the Block Exemption Regulation to the extent that promotion on the internet or use of the internet would lead to active selling into, for instance, other distributors' exclusive territories or customer groups. The Commission considers online advertisement specifically addressed to certain customers as a form of active selling to those customers. For instance, territory-based banners on third party websites are a form of active sales into the territory where these banners are shown. In general, efforts to be found specifically in a certain territory or by a certain customer group is active selling into that territory or to that customer group. For instance, paying a search engine or online advertisement provider to have advertisements displayed specifically to users in a particular territory is active selling into that territory*".

practical experience with the distinction between active and passive sales in the context of internet sales. The feedback we received from a wide range of jurisdictions was that the Contributing Practitioners do not take any risk in this area and therefore in their practice do not rely upon paragraphs 52-53 of the Vertical Guidelines to qualify certain online sales as active sales. This response to our (albeit limited) inquiry is consistent with our own practice. While we appreciate that a distinction can be made between active and passive selling in the online world, the reality is that in our experience practitioners tend to treat online sales systematically as passive sales. The sensitivity (hardcore) of the issues of online sales combined with territorial restrictions render any other approach on the part of practitioners too risky.

Based upon the feedback of the Contributing Practitioners and our own practice, the Commission's study would lend support for the proposition that, depending on the product categories involved, a very substantial part and sometimes more than half of the sales (being internet sales) may qualify as passive sales that cannot be restricted.

Such fact-finding is highly relevant when evaluating the possible negative effects of active sales restrictions under the current VBER regime. There seem to be two immediate conclusions that can be factored into the assessment for the future. *First*, with the increase in online sales the possible negative effects resulting from an active sale restriction in an exclusive distribution system may be deemed to have decreased compared to the time when Regulations 2790/99 and 330/2010 were adopted. If online sales are in practice treated systematically as passive sales (which, in our understanding, is what practitioners and businesses tend to do), the proportion of the business that is affected by an active sales restriction has gone down due to the relative increase of online selling compared to offline selling. This implies also that that the (potentially negative) impact of active sales restrictions on intra-brand competition and possibly consumer welfare has gone down and similarly that the risk that obstacles to market integration and price differences between different territories can be maintained has likewise gone down. *Second*, on account of the differences in the relative importance of online sales depending on the products involved, the potential negative effects of active sales restrictions are not product-neutral. Those effects will be less in sectors where online sales are more prevalent. While this second observation may not necessitate a change in policy approach, it underscores that the starting point of the analysis that is reflected in the Vertical Guidelines (paragraph 163) may no longer be valid.

Given the above, it should not come as a surprise that in our practice the impact of online selling has completely overshadowed the previously held debates on active sales and the restriction thereof. In most cases, when free-riding concerns are expressed, they relate to online sales and not (or at least not to the same extent) to active (as opposed to passive) selling engaged in by another trader in the offline world.

2. The impact of inter-brand competition and the remaining intra-brand competition

In respect of the impact of vertical restrictions on intra-brand competition, it is generally put forward in economic literature[11] and also acknowledged in the Vertical Guidelines (paragraph 153) that "*the loss of intra-brand competition can only be problematic if inter-brand competition is limited*". The Vertical Guidelines (paragraph 154) furthermore provide that "*[s]trong competitors will generally mean that the*

[11] S. BISHOP and M. WALKER, *The Economics of EC Competition Law: Concepts, Application and Measurement*, third edition, Sweet & Maxwell, 2010, page 195.

reduction in intra-brand competition is outweighed by sufficient inter-brand competition".

It seems therefore difficult to deny that possible negative effects of an active sales restriction on intra-brand competition may be counterbalanced by sufficient inter-brand competition. The market position of both the suppliers and distributor(s) will be a relevant factor to ensure sufficient inter-brand competition. This is currently achieved by the application of the market share limit of 30% under the VBER.

The structure of the market is deemed a relevant factor when determining the extent of inter-brand competition either at supplier or distributor level. The Vertical Guidelines refer in this respect to the negative cumulative effects of multiple exclusive dealerships, where the same distributor is appointed by different suppliers[12], either at wholesale level[13] or retail level[14]. The purpose of Article 6 of Regulation 330/2010 is precisely to address such cumulative effects so that, with the non-application system already included in the VBER, the risk of cumulative effects should not be decisive for the assessment of the future regime of active sales restrictions.

Other factors mentioned in the Vertical Guidelines are the maturity level of the market (paragraph 158) and the level of trade (wholesale or retail level) coupled with the size of the territory covered by the exclusivity (paragraph 159). However, if the 30% market share limit is maintained, these factors would not seem a sufficient reason to adopt a differentiated approach in the revised VBER (based on factors such as the level of trade or the maturity level) towards active sales restrictions.

Under the current VBER regime, distributors cannot be prevented from engaging in passive sales and customers of the distributors are not restricted from selling goods – actively or passively – in certain markets or to certain customers. This implies that, in addition to the impact of inter-brand competition, there will be remaining intra-brand competition that has an impact on the possible negative effects of active sales restrictions.

Hence, when assessing the negative effects of active sales restrictions for purposes of considering the different Policy Options under the revised VBER, the combination of inter-brand competition and the remaining intra-brand competition must be taken into consideration. As stated in point 1 above, the impact of the freedom to engage in internet selling (which practitioners and businesses tend to qualify as passive selling) in the exclusive territory/towards the exclusive customer group by other distributors

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[12] Vertical Guidelines, paragraph 154: "*[…] Multiple exclusive dealerships, that is, when different suppliers appoint the same exclusive distributor in a given territory, may further increase the risk of collusion and/or softening of competition. If a dealer is granted the exclusive right to distribute two or more important competing products in the same territory, inter-brand competition may be substantially restricted for those brands. The higher the cumulative market share of the brands distributed by the exclusive multiple brand dealers, the higher the risk of collusion and/or softening of competition and the more inter-brand competition will be reduced*".

[13] Vertical Guidelines, paragraph 160: "*[…] The possible risks for inter-brand competition of multiple exclusive dealerships are however higher at the wholesale than at the retail level. Where one wholesaler becomes the exclusive distributor for a significant number of suppliers, not only is there a risk that competition between these brands is reduced, but also that there is foreclosure at the wholesale level of trade*".

[14] Vertical Guidelines, paragraph 154: "*[…] If a retailer is the exclusive distributor for a number of brands this may have as result that if one producer cuts the wholesale price for its brand, the exclusive retailer will not be eager to transmit this price cut to the final consumer as it would reduce its sale and profits made with the other brands. Hence, compared to the situation without multiple exclusive dealerships, producers have a reduced interest in entering into price competition with one another […]r*".

and the increased levels of such internet sales should be duly considered when drawing appropriate conclusions in respect of the Policy Options.[15]

3. The economic rationale for pursuing market integration

The Vertical Guidelines (paragraph 7) mention the creation of obstacles to market integration, facilitating price discrimination, as a distinct negative effect. They provide that "*[a]ssessing vertical restraints is also important in the context of the wider objective of achieving an integrated internal market. Market integration enhances competition in the European Union. Companies should not be allowed to re-establish private barriers between Member States where State barriers have been successfully abolished*".

There is indeed some tension between territorial sales restrictions, such as active sales restrictions, reducing cross-border trade between Member States and the more general internal market objective of the EU.[16] In economic literature, obstacles to market integration created by vertical restraints are often not thought to be grounded in economics, but are mainly deemed to relate to the realization of the EU policy objective of the single European market.[17] Certain authors therefore observe that reliance on the negative effects of active sales restrictions on market integration, does not necessarily sit well with pursuing economic efficiency and consumer welfare.[18]

Such criticism may not be fully justified. The Vertical Guidelines (paragraph 151) express the market integration concern also differently by referring to market partitioning, which may facilitate price discrimination in particular. The internal market objective can therefore in economic terms be translated into the negative effects caused by price discrimination, which in turn affects consumer welfare.

Hence, when considering the Vertical Guidelines in their totality, we do not believe that the criticism in respect of economic effects with reference to the market integration objective is really accurate. It remains relevant to consider the impact of active sales restrictions on market partitioning and price discrimination. These aspects are particularly relevant in order to include properly the consumer perspective in the evaluation of the Policy Options.

4. Negative effects and business practice

To the extent that our practice and that of the Contributing Practitioners of the past years can be considered a relevant yardstick to assess the negative effects of active sales restrictions, we find that there is a genuine risk of overstating the ability of active sales restrictions to trigger the negative effects put forward in the Vertical Guidelines. Any such appreciable negative effects seem more logically related to the concept of exclusive distribution (exclusive appointment, possibly combined with location clauses). We have seldom encountered cases where one or several negative

[15] This conclusion is confirmed by the findings in the evaluation study regarding the impact of e-commerce growth on exclusive distribution networks in the Commission Staff Working Document on the Evaluation of the VBER, page 38.

[16] M. DE LA MANO and A. JONES, "Vertical Agreements under EU Competition Law: Proposals for Pushing Article 101 Analysis, and the Modernization Process, to a Logical Conclusion", King's College London Law School Research Paper, nr. 2017-23, page 11.

[17] G. NIELS, H. JENKINS and J. KAVANAGH, *Economics for Competition Lawyers*, second edition, Oxford University Press, 2016, page 289; E. ELHAUGE and D. GERADIN, *Global Antitrust Law and Economics*, second edition, Foundation Press, 2011, page 700.

[18] S. BISHOP and M. WALKER, *The Economics of EC Competition Law: Concepts, Application and Measurement*, third edition, Sweet & Maxwell, 2010, page 206.

effects (appreciable limitations of intra-brand competition or the creation of genuine obstacles to market integration) could be traced back specifically to the imposition of active sales restrictions. In this respect, the discussion of the negative effects in the Vertical Guidelines under the broader heading of "exclusive distribution" and not specifically under a heading of "active sales restrictions" seems fully justified.

Another way of measuring the possible existence of negative effects in actual practice is to consider the number of cases where we or the Contributing Practitioners have been contacted by distributors that felt constrained by an active sales restriction (and wished to challenge its enforceability) or by suppliers that wanted to enforce such a restriction. The number of such business cases is very low and represents a minimal part of our practice in the area of vertical agreements. Based on the sources that are available to us, the same conclusion would result from the lack of enforcement practice and the limited case law in this area.

On account of the foregoing, our practice of the past 10 years and that of the Contributing Practitioners do not offer support for a proposition that, in practice, active sales restrictions have triggered appreciable negative effects to competition in general and negative consequences for consumer welfare in particular.

B. Positive effects of active sales restrictions

The Vertical Guidelines (paragraph 107) list the following grounds which may justify exclusive distribution: (i) free-rider problems; (ii) new market entrance; (iii) the 'certification free-rider issue'; (iv) the hold-up problem when client-specific investments are made, (v) the vertical externality issue, and (vi) economies of scale in distribution. It does not specifically do so for the use of active sales restrictions. However, for purposes of this Report, these grounds were assessed on the assumption that exclusive distribution implies the imposition of active sales restrictions.

- **Free-rider problem**: The free-rider problem is an issue that suppliers may encounter within their distribution systems. A supplier will want its distributors to make investments and undertake promotional efforts, but a distributor will only be willing to do so, if its efforts are to its own benefit and are not undermined by other distributors free riding on its efforts. The fear for free riding therefore risks undermining the efficient introduction and distribution of a supplier's products, as it may prevent that the necessary sales efforts are made. Exclusive distribution including active sales restrictions may help to overcome this issue by protecting (to a certain extent) sales resulting from investments (e.g., publicity, pre-sales services, etc.) in a certain area or towards a certain customer group.[19] This will normally not extend to free-riding concerns stemming from online sales as, in practice, such sales will be deemed passive sales.

  The Vertical Guidelines mention that a real free-riding issue can only exist in respect of pre-sales services and other promotional activities, but not, for example, for post-sales services for which the distributor can charge the customer individually. It may be useful to add the following observations to this:

  - *First*, it is relevant to note that certain economic literature has advanced that the free-rider justification for an active sales restriction in respect of certain pre-sales services may in certain sectors be outdated, for example, when pre-sales services such as product demonstrations, reviews, user guides, etc. are easily accessible

[19] E. ELHAUGE and D. GERADIN, *Global Antitrust Law and Economics*, second edition, Foundation Press, 2011, page 700.

online.[20] It will also be relevant to take into account the findings of the support study of the Commission on consumer purchasing behaviour in Europe[21], and more particularly the different channels that are used by customers for inspiration, information and evaluation of a purchase. Whether the free-riding issue can effectively be addressed by an active sales restriction would therefore seem to depend on the extent to which pre-sales services and promotional efforts for the specific product/in the specific sector are still undertaken by the exclusive distributor. It may be assumed that suppliers will be more receptive to demands for exclusivity by distributors if they make investments and where there is a genuine free-riding risk.

- *Next*, based on our experience, we are not necessarily convinced by the observation that there can only be a risk of free riding for pre-sales efforts and not for after-sales services for which customers can be charged individually. Such a clear split does not necessarily match with our practice. The reality is that in certain sectors (typically involving rather expensive and complex products) a considerable investment is required in order to perform after-sales services up to the required standards set by the supplier. The fact that the distributor can charge the customer separately for the after-sales services does not necessarily solve the free-rider issue. The risk the distributor is facing is that a competing distributor is making less investments in the after-sales business (tooling, equipment, parts, inventory, training, personnel, logistics and the like) and counts on the fact that other distributors will do so and be available to handle (complex) after-sales support. The latter distributor can price the products more sharply (for not having made the same after-sales investments) and the investing distributor will have less sales of the primary products on the basis of which its after-sales investments can be recovered. A distributor may therefore only be willing to make such after-sales investments if it has some certainty that it will be able to attract enough customers for the primary products so as to create a relationship with the customer for future after-sales support.[22] In addition such sale of primary products may also assist in recovering at least part of the investments relating to after-sales support. A typical counter-argument is that suppliers can avoid this problem by imposing relevant after-sales requirements and standards in their agreements. While this is correct in theory, our practice shows that this will depend on the balance of power between the supplier and the distributor.

- **New market entrance**: The issue relating to opening up or entering new markets concerns a special case of the free-rider problem. A supplier who wishes to enter new markets will need to convince a distributor to invest in

[20] G. NIELS, H. JENKINS and J. KAVANAGH, *Economics for Competition Lawyers*, second edition, Oxford University Press, 2016, page 276.

[21] Commission, *Support studies for the evaluation of the VBER – final report*, Publications Office of the European Union, 2020, available at https://op.europa.eu/en/publication-detail/-/publication/93f52e95-a92e-11ea-bb7a-01aa75ed71a1.

[22] For instance, in the automotive sector it is well known that the vehicles covered by direct sales efforts by the importer are *de facto* delivered by the local dealer in order to establish a direct customer relationship for after-sales services.

the new territory or customer group. A distributor may however only be prepared to do so if it is able to enjoy some protection in the new territory or towards the new customer group.[23]

Our practice confirms that exclusive distribution is considered in such a scenario, in particular where a supplier wishes to expand its activities from its home or well-developed markets into new markets. An active sales restriction may in those circumstances be requested by a distributor in return for the investments in the brand or the products. In such cases, the balance of power between the supplier and the distributor is often such that the distributor is well positioned to negotiate this type of protection.

- The **certification free-rider issue**: The Vertical Guidelines also mention the need in certain sectors to sell via retailers who have a reputation for stocking only quality products to allow the introduction of a new product. Reference is made in the Vertical Guidelines to exclusive distribution as an appropriate solution to ensure that products are sold via reputable retailers.

  Based on our experience, we do not believe that exclusive distribution always offers an efficient solution for this issue. In an exclusive distribution set-up and due to the rolling over prohibition, a supplier only has control over the first distribution level with which it contracts (see, paragraphs 0-0 below). The subsequent levels (sales by the exclusive distributor to other buyers and onwards) and parallel trade into the exclusive territory are outside the control of the supplier. Therefore, contrary to selective distribution, a product distributed via exclusive distribution runs the risk of losing its premium brand image on account of sales through such alternative distribution channels. Hence, when this issue has come up in our practice, the more obvious solution has been to opt for selective distribution and not to recommend exclusive distribution coupled with active sales restrictions.

- The **hold-up problem**: The hold-up problem concerns the situation where a distributor is required to make specific investments, which it is not willing to make unless benefitting from a certain protection. The Vertical Guidelines mention that, in such a case, exclusive distribution may provide an appropriate solution.

  As stated in the Vertical Guidelines, the hold-up problem requires very specific circumstances. We did not come across any relevant examples in our advisory practice, nor have the Contributing Practitioners, where this issue was resolved by means of an active sales restriction. In such a scenario, a sufficiently developed system of location clauses offers more tailored protection of the investments than an active sales restriction.

- **Vertical externality issue**: A negative vertical externality issue may exist for the supplier when a retailer is making too little sales efforts, but where additional efforts would result in additional sales and more benefits to the supplier.

  In our experience, we have not come across business cases where exclusive distribution, including an active sales restriction, offered a solution for a vertical externality issue as defined in the Vertical Guidelines (paragraph 107(f)). The Contributing Practitioners have also not brought any such cases to our attention.

[23] G. NIELS, H. JENKINS and J. KAVANAGH, *Economics for Competition Lawyers*, second edition, Oxford University Press, 2016, page 279.

- **Economies of scale**: The concentration of the resale of products by means of exclusive distribution may result in economies of scale. We are not really aware of relevant business cases, where protection against active sales was chosen by the supplier to ensure economies of scale. We have rather seen business cases where the exclusivity of appointment in combination with the geographic scope of the contract territory played an important role to secure economies of scale.

  An example from our practice is a case where a supplier wanted to set up an efficient after-sales network by generating certain economies of scale. To that end, the supplier appointed a single service center with which it contracted and required that center to establish (independent) sub-centers across its region. The service center was responsible for stocking parts and supplying them to the sub-centers, providing training to the sub-centers and solving complex repair issues which the sub-centers were unable to handle themselves. The exclusivity granted to the service center for the region was important to cause it to accept this particular role and thus to generate the efficiencies of scale. Protection against active selling did not really play a role in this respect, even though on account of the nature of the products to be serviced competition from out-of-territory service providers was perfectly possible. It was rather the contractual guarantee that no other service center would be appointed within the region that caused the center to assume this role.

It is not so easy to link our experience to the positive theories advanced in the Vertical Guidelines. In our practice, requests for exclusivity were essentially triggered by the need to encourage distributors to make investments specifically geared towards the products of the supplier. The need to ensure enough business in order to justify such investment efforts was often driving the request. The fear that other distributors may somehow free ride on the investments was sometimes a factor, but in our experience to a much lesser extent than the need (as such) to secure a certain volume of business by means of territorial exclusivity. Unsurprisingly, a crucial role in the discussions between the supplier and the distributor in this respect is played by the size of the territory. Active sales restrictions could be conceived as an additional motivation for the distributor to make the required investments, but they will not be as decisive as, for instance, the geographic scope of the exclusive territory. The difficulties related to the VBER regime governing active sales restrictions, which will be addressed in detail further in this Report, are in our experience a very important factor undermining the attractiveness of this type of restrictions for the protection of investments.

In this context, the concept of investments must in our experience be understood broadly. In many sectors a significant part of the investment will be in time, training (familiarity with the products, after-sales support, etc.) and focus (well-performing distributors are often selective in the number of brands they wish to handle). The relevant investments are therefore not necessarily confined to financial investments in hardware or software. In certain sectors the non-financial investments are often more important for the supplier. Furthermore, while investments in hardware or software are more of a one-off or less frequent nature, the non-financial investments are in most cases permanent throughout the distribution relationship.

Genuine concerns about discrepancies between investment levels and risks of free riding were in our experience for the most part not resolved by means of exclusive distribution, but by selective distribution. Selective distribution makes it possible to ensure that all of the distributors are making not necessarily identical, but comparable investments and that no products can be leaked to traders not making such investments. If this risk reflects a genuine business concern and as the law stands,

exclusive distribution does not necessarily provide the most appropriate answer, because it does not rule out activities of traders (e.g., pure box movers) not making comparable investments. Hence, we have noticed increasingly that businesses switch from a (often less formalized) system of non-exclusive distribution to selective distribution, rather than to exclusive distribution in order to encourage and protect investments made by the network.[24]

Turning to active sales restrictions more specifically, it will very much depend on the sector (and the products involved) whether they may contribute significantly to the protection of the investments and the creation of business volumes that may justify such investments. In sectors that are characterized by significant internet selling, the limitation of the ability to engage in active selling (typically a restriction of offline sales) will not be perceived as a major contribution in addition to exclusivity, possibly combined with location clauses imposed on other distributors. Active sales restrictions will most likely only be perceived as a factor of significance if active and targeted offline marketing presents an effective way of persuading customers to purchase from a different distributor than those they would approach naturally, for example, on account of their physical location.

C. Conclusions

Based on our experience, we perceive a genuine risk of overstating both the negative and the positive effects associated with active sales restrictions.

With regard to possible negative effects, the current VBER regime requires the freedom to engage in passive sales and leaves the second and subsequent tiers free to engage both in active and passive sales. Hence, the regime contains so much room for continued intra-brand competition across territories that it would be inaccurate to overstate possible negative consequences. If anything, such consequences are possibly more attached to the concepts of territorial exclusivity and location clauses and not necessarily to active sales restrictions.

With regard to the possible positive effects, it will depend on the sector and the products involved whether active sales restrictions may be perceived as a useful tool to incite and protect investments. This will most likely depend on the extent to which active and targeted offline marketing is effective to cause customers to switch. The supplier has only an interest in granting such protection if it triggers investments that would otherwise not be made or not to the same extent, and the distributor will only benefit from this type of protection if it makes a difference for its willingness to invest.

V. Overview of current regime

This chapter touches briefly upon the cases where territorial restrictions (including active sales restrictions) may escape the application of Article 101(1) TFEU (see, section A). This is followed by a description of the relevance of the chosen distribution formula when imposing an active sales restriction in the context of the VBER (see, section B). Next, certain key concepts merit specific attention given their importance for the application of the current regime (see, section C). Finally, the chapter provides an overview of the current VBER regime governing the imposition of active sales restrictions (see, section D). The issue of active sales restrictions represents presumably one of the most complex aspects of the VBER.

[24] Our experience seems to be in line with the finding of the NCAs that "*cases involving exclusive distribution were not very numerous during the analysed time period*" as mentioned in the Commission Staff Working Document on the Evaluation of the VBER, page 62.

A. Territorial restrictions falling outside of Article 101(1) TFEU

The Vertical Guidelines (paragraphs 61-62) cite two examples where territorial restrictions imposed in distribution agreements that are listed in Article 4 of Regulation 330/2010 do nevertheless escape the application of Article 101(1) TFEU. The first example (paragraph 61) concerns investments made to enter a market either to sell a new brand or to be the first to sell an existing brand on that market. In order to facilitate the recoupment of the investments, the distributor can under certain conditions receive protection against active and passive selling by other distributors and this for a limited period of time. The second example (paragraph 62) concerns genuine testing of a new product in a limited territory or with a limited customer group and the case of a staggered introduction of a new product. In these scenarios the distributor appointed to conduct the test or to perform the introduction may be limited in its active sales outside the market for the period needed for the testing or introduction.

Our understanding is that the first example relies in any event on the objective justification theory and that the second example may rely either on the ancillary restraints doctrine or the objective justification theory.[25] This is however not entirely clear from the Vertical Guidelines.

From a practical perspective, these scenarios trigger two fundamental questions:

- The first question is whether a territorial restriction that falls outside Article 101(1) TFEU still qualifies as a hardcore restriction within the meaning of Article 4 of Regulation 330/2010. The language of the Vertical Guidelines[26] and the Article 101(3) Guidelines[27] point in that direction. If that is the case, the inclusion of such a non-restrictive territorial limitation excludes the application of the block exemption to the relevant distribution agreement(s) in its (their) entirety. Such a position renders these scenarios completely unworkable. Considering the first scenario (paragraph 61 of the Vertical Guidelines), the relevant active and passive sales restrictions are to be included in other distribution agreements than that which benefit from the protection. Why would distributors accept such restrictions if they put the applicability of the block exemption and hence the enforceability of all of the other restrictions included in their own distribution agreements potentially at risk? The only solution that renders these exceptions meaningful is to provide explicitly that the non-restrictive limitations do not qualify as hardcore restrictions so that they do not trigger the unhelpful consequences referred to above.
- The second question concerns the proper interpretation of the conditions that bring these scenarios into play. The first case (paragraph 61 of the Vertical Guidelines) refers to "*substantial investments*", "*previously no demand*", "*necessary*", "*a certain period of time*" which in the example (without further

[25] F. WIJCKMANS and F. TUYTSCHAEVER, *Vertical Agreements in EU Competition Law,* third edition, Oxford University Press, 2018, page 173, paragraph 6.07, page 181, paragraph 6.35 and page 324, paragraph 9.230.

[26] Vertical Guidelines, paragraph 60: "*Hardcore restrictions may be objectively necessary in exceptional cases for an agreement of a particular type or nature and therefore fall outside Article 101(1) […]*".

[27] Guidelines on the application of Article 81(3) of the Treaty [2004] OJ C101/97, footnote 24: "*See rule 10 in paragraph 119 of the Guidelines on vertical restraints cited in note above, according to which inter alia passive sales restrictions — a hardcore restraint — are held to fall outside Article 81(1) for a period of 2 years when the restraint is linked to opening up new product or geographic markets*".

clarification) is defined as "*the first two years*", etc. The second case (paragraph 62 of the Vertical Guidelines) refers to "*genuine testing*", "*staggered introduction*", "*necessary for the testing or introduction of the product*", etc. All such concepts leave quite some room for interpretation and hence present a considerable risk that, rather than being non-restrictive, the limitations are deemed to infringe Article 101(1) TFEU and are not block exempted.

The combination of these two fundamental questions renders these exceptions unattractive and unworkable. In our practice we do not advise to make use of these exceptions. The border line between the inapplicability of Article 101(1) TFEU and the hardcore regime is simply too unclear. Furthermore, the risk that even when falling outside of Article 101(1) TFEU the limitations are qualified as hardcore restrictions that attract all the related negative consequences (such as the inapplicability of the block exemption to the whole of the agreement and the negative presumption related to a possible individual exemption) is simply too high a price. As stated, such a price is unrealistically high all the more if the relevant limitations are to be included in distribution agreements entered into by distributors that do not benefit from the related protection (paragraph 61 of the Vertical Guidelines).

B. Relevance of chosen distribution formula in the context of VBER

The treatment of active sales restrictions in the VBER differs depending on the chosen distribution formula. The key distinction is that between selective and non-selective distribution agreements. For purposes of the present overview, a non-selective distribution agreement can be defined as any type of distribution agreement that fails to meet the requirements of a selective distribution agreement stated in Article 1(1)(e) of Regulation 330/2010.

Active sales restrictions limiting a distributor's activities towards an exclusively allocated or reserved territory are in the current regime only block exempted in the case of non-selective distribution agreements. In a selective distribution network it is not possible to restrict the territorial activities (both in terms of active and passive selling) of the members of the network (Article 4(c) of Regulation 330/2010). The Vertical Guidelines (paragraph 56) leave room for a limited exception to this general principle in case the supplier does not apply a selective distribution system across the whole of the EEA (hybrid scenario).

The position is different with regard to customer restrictions. It is common to selective and non-selective distribution agreements that wholesalers can be restricted in their sales to end users (Article 4(b)(ii) of Regulation 330/2010). This can even take the form of an outright ban (covering both active and passive selling).

The regime governing customer restrictions is different for the two formulas (selective/non-selective) in the following respects:

- Subject to certain conditions (that will be discussed below) the VBER permits the imposition in non-selective distribution agreements of active sales restrictions towards certain customer groups. Passive sales restrictions are in any event not covered by the block exemption.
- As an integral part of the definition of a selective distribution agreement, distributors are bound to accept a prohibition on sales to unauthorized distributors (Articles 1(1)(e) and 4(b)(iii) of Regulation 330/2010). This prohibition covers both active and passive sales.
- With a limited exception (that will be discussed below) the VBER does not exempt the imposition of active sales restrictions in a selective distribution agreement towards customers other than unauthorized distributors.

The focal point of the overview of the current regime described in this Report is the imposition of active sales restrictions in accordance with Article 4(b)(i) of Regulation 330/2010, which covers both territorial and customer restrictions in a non-selective environment. The Report encompasses also active sales restrictions imposed in selective distribution agreements towards non-selective territories (hybrid scenario), provided that certain requirements are met.

C. Certain key concepts

For the purposes of the present Report, there are a number of key concepts that may require clarification. They are instrumental in understanding and evaluating the current approach towards active sales restrictions.

1. Active and passive sales

'Active sales' as opposed to 'passive sales' obviously occupy a central place. These concepts are defined in paragraph 51 of the Vertical Guidelines. At the risk of oversimplifying matters, active sales imply targeted sales efforts to reach a specific customer group or territory. General sales efforts that remain attractive to a buyer even if a particular customer group or territory is not reached, may be considered passive sales as regards such a customer group or territory.

Both in our own practice and in that of the Contributing Practitioners we have not found many cases where these concepts present real interpretation difficulties in the offline world.[28] The distinction between active or passive offline sales seems rather clear. In practice, the difficulties that have been reported are more of an evidentiary nature. Most often, the supplier will not be able to collect conclusive documentary evidence that the sale resulted from targeted sales efforts by a distributor. The distributor will obviously have no interest in supporting the supplier in its attempt to meet its burden of proof. In the online world, the distinction between active and passive selling poses more difficulties. While there is a brief reference to the internet in the description of active selling in the Vertical Guidelines (paragraph 51), many Contributing Practitioners refer to the need to create greater clarity on the dividing line between active and passive selling in the online world. A limited inquiry with the Contributing Practitioners indicates that they treat internet sales in practice systematically as passive sales in order to avoid any risk of an incorrect qualification and the related hardcore problem. This finding is consistent with our own practice (see, paragraph 0 above).[29]

It is our understanding that there will be a separate Expert Report dealing with e-commerce and that these concepts are likely to be addressed in detail there. For present purposes, it may suffice that it is not entirely clear whether it is the actual distinction between active and passive selling that presents the greatest practical difficulty. It is our impression that the more relevant issue for this Report is that in practice passive selling has gained a totally different meaning and importance as a result of the surge of online selling.

In the offline world, passive selling typically requires a real effort on the part of the customer (often combined with the need to travel to the relevant location) that is not

[28] An interesting example mentioned by one of the Contributing Practitioners that may give rise to questions of interpretation is that of a market which is characterized by public or private tenders. A similar question is mentioned in the Commission Staff Working Document on the Evaluation of the VBER, page 125.

[29] The importance of the distinction between active and passive sales to avoid a hardcore restriction under the VBER was also stressed by some respondents in the evaluation phase (Commission Staff Working Document on the Evaluation of the VBER, page 215).

comparable to the (very limited) effort that is required to explore possibilities on the internet. Hence, the business impact of the distinction between active and passive selling has shifted considerably with the increased use of the internet. As already explained in paragraphs 0-0 above, the prohibition of active selling provides less protection in an environment where an important part of the sales are internet sales as such sales are, in practice, characterized as passive sales that are not caught by any active sales restriction.[30]

2. Exclusively allocated, customer group and reserved for the supplier

The concept of 'exclusivity' is used in Article 4(b)(i) of Regulation 330/2010 and is given a particular meaning in paragraph 51 of the Vertical Guidelines. The constituent elements are further discussed in section D below.

A question on which the Vertical Guidelines do not offer guidance is whether exclusivity must be contractually pre-determined and stable or whether it can be established *ad hoc* at the request of a distributor and be temporary in nature. This question is tied in with a proper understanding of the notion of "allocated" that is used in Article 4(b)(i) of Regulation 330/2010, *i.e.*, what it is that is needed in order to meet the requirement that an exclusive territory or an exclusive customer group is "allocated" to a given buyer.

The issue has come up in a Latvian case in the context of a registration system whereby a distributor enjoys protection against active selling to registered customers during a limited period of time (typically six months).[31] The question is likely to be addressed in the preliminary ruling to be rendered in that matter.

The Latvian case concerns a concept that we have encountered in our own practice. It comes up in a context and in sectors where there are considerable pre-sales efforts in order to get a customer interested in a possible commercial transaction. Typical examples are cases where the distributor has to conduct lots of measurements, needs to make an on-site visit or prepares drawings with regard to tailor-made solutions. In many instances customers will not pay for such work or, if they do, the fee that can be charged is rather symbolic compared to the hours spent. In order to limit the risk of free riding on these efforts, the distributor that has performed the work is allowed to register the customer and the other distributors accept contractually not to engage in active selling towards such customer for a limited period of time.

Apart from whether such a scenario meets the standard of 'allocation' envisaged in Article 4(b)(i) of Regulation 330/2010, it also triggers the question whether a 'customer' or a 'customer group' is involved. The latter question seems (at least *prima facie*) important as the exception included in Article 4(b)(i) of Regulation 330/2010 is linked to an 'exclusive customer group'. On the notion of 'customer group', the Vertical Guidelines do not offer any particular clarification.[32]

It is not so difficult to formulate this scenario in such a manner that it, on any reasonable reading of the distribution agreement, should fall within the exception. If the distribution agreement provides that the relevant exclusive customer group consists of such customers for which the distributor has performed specified pre-sales

[30] This finding follows from our practice and is supported by findings in the evaluation study regarding the impact of e-commerce growth on exclusive distribution networks in the Commission Staff Working Document on the Evaluation of the VBER, page 38.

[31] Case C-306/20, *SIA Visma Enterprise/Competition Council Latvia*.

[32] Other language versions seem to distinguish likewise between 'customer' and 'customer group'. The French version refers to "*clients*" and "*clientèle*" and the German version to "*Kunden*" and "*Kundengruppen*".

services (such as the performance of drawings of a tailor-made solution) and that have been registered subsequently in a tool that is accessible to all of the distributors, we fail to see why the test of Article 4(b)(i) of Regulation 330/2010 (both as regards the issue of 'allocation' and 'customer group') would not be met.

Also the economic logic underpinning Article 4(b)(i) of Regulation 330/2010 supports such a conclusion. This is a clear case where there is a properly identifiable risk of free riding and where, in addition, the allocated customer group is narrowly defined (both in terms of members of the group and the time during which they belong to the group). This approach implies that the restriction of active selling is more targeted and therefore more limited than in many other cases where customer groups are more broadly or generically defined and the free-riding risk may not present itself for each and every member of the group thus defined.[33]

Similar considerations apply to the concept of an 'exclusive customer group reserved to the supplier'. Imagine a scenario where the supplier wishes to reserve a single (e.g., large multinational) customer for itself on account of the longstanding relationship with that customer and the considerable efforts previously made to acquire and retain the customer. In this case it will be somewhat more difficult, but doable to draft the relevant provision in such a manner that this single customer qualifies as a 'customer group'. One way of doing so would be to define the customer group as that particular multinational and such other multinationals as the supplier may communicate from time to time to the distribution network. All of this goes to show that the distinction between 'customer' and 'customer group' may be more formalistic than real and that, in order to limit the active sales restrictions to the actual situations where there is a proper economic and business justification, it may make sense to apply the exception to cases where a single customer is involved and to avoid contract drafting aimed at placing such a customer in a customer group.

In addition and similarly to the concept of 'allocation', there is the question of when a supplier has done enough to 'reserve' a customer group or territory to itself. Is it necessary that this is part of the distribution agreement or are less formal ways of doing so acceptable (e.g., in an exchange of correspondence)? Similarly, does the notion of reservation imply that the network is informed in detail of the territories or customer groups concerned or does it suffice that the distributor can reach out to the supplier, in case it wishes to approach a new territory or customer, in order to find out whether any such reservation applies?

All of this goes to say that the notions of 'allocated', 'reserved' and 'customer group' may give rise to issues of interpretation. These issues are not merely theoretical and have come up in our practice. It may therefore be useful to consider offering additional guidance in the future Vertical Guidelines. This is particularly so if DG Competition were to decide that these notions include certain requirements (formal or other) that may limit the scope of application of the exception contained in Article 4(b)(i) of Regulation 330/2010.

[33] The question can be raised whether such a system will in practice not result in absolute customer protection (covering both active and passive selling). We fail to see how the position in respect of this particular hypothesis is necessarily different from other scenarios where active selling is restricted and passive selling must be left free. A difference is that the restriction in this particular case is much more narrowly circumscribed so that, if in practice the restriction extends to passive selling, the relevant customer comes "free" more quickly and the group affected by the restriction is narrower, leaving both active and passive selling unaffected for all similar customers that have not been registered.

3. Location clause

Article 4(b) of Regulation 330/2010 carves out location clauses from the hardcore list. This concept is clarified in paragraph 50, *in fine*, of the Vertical Guidelines. It is a broad concept that covers both outlets and warehouses and both primary and additional locations. It also permits that any change or addition is rendered subject to the prior approval of the supplier, whereby the supplier has discretion in granting or refusing such consent.

Location clauses are typically considered from the perspective of the distribution agreements in which they are imposed. However, the block exemption also permits the supplier to provide a contractual guarantee to a given distributor that another distributor is subject to, and will remain subject to a location clause. The territorial protection against free riding is offered by the latter guarantee and the imposition of the location clause is no more than an execution of such guarantee.

Location clauses, when properly understood, are an important tool to address free-riding concerns. In our experience and in the experience of certain Contributing Practitioners, location clauses have in certain specific sectors, where online sales are less prevalent, proven to be of greater value than active sales restrictions. If there is uncertainty as to whether all the conditions can be met to keep the active sales restriction off the hardcore list, there is often an additional incentive to work with location clauses and to avoid the complexities inherent in setting up a compliant active sales restriction regime.

For purposes of this Report, the treatment of location clauses should therefore constitute an integral part of the overall debate on the future of territorial restrictions in the new block exemption regime.

4. Geographic scope of Article 4(b) of Regulation 330/2010

A final point that is worth raising concerns the geographic scope of the hardcore provision contained in Article 4(b) of Regulation 330/2010. This point is not explicitly addressed in the VBER and some guidance, albeit somewhat hidden, is offered in the Vertical Guidelines. During exploratory talks in the context of the preparation of the VBER we shared with DG Competition our concern that the geographic scope was in our practice an unnecessary point of debate or contention. This point is now addressed in footnote 5, paragraph 47 of the Vertical Guidelines, including a quote from *Javico*.[34] Our practice shows that this footnote is often unknown and therefore has not resolved the uncertainty that exists in business circles and legal departments. As distribution networks often extend beyond the EEA borders and given the new situation resulting from Brexit, stakeholders would benefit from more explicit treatment of the geographic dimension of Article 4 of Regulation 330/2010 either in the future Regulation or the future Vertical Guidelines.

D. Conditions for the application of Article 4(b)(i) of Regulation 330/2010

Active sales restrictions included in non-selective distribution agreements are block exempted subject to a number of cumulative conditions. Since these conditions are of critical importance for a proper assessment of the experience with the current VBER regime, they will be addressed in some detail below:

[34] Case C-306/96, *Javico*, ECLI:EU:C:1998:173, paragraph 20: "*[…] an agreement in which the reseller gives to the producer an undertaking that he will sell the contractual products on a market outside the Community cannot be regarded as having the object of appreciably restricting competition within the common market or as being capable of affecting, as such, trade between Member States*".

1. Characteristics of the target territory/customer group

Different from certain previous block exemption regimes (see, e.g., Regulation 1983/83), the characteristics of the territory in which the distributor is located or active is irrelevant in order to determine whether it can be subjected to an active sales restriction. Also non-exclusive distributors can be subjected to active sales restrictions. It is the 'exclusive' characteristic of the target territory (the 'protected' territory) that determines whether the requirements of Article 4(b)(i) of Regulation 330/2010 are met.[35]

A first scenario is that the target territory is an "*exclusive territory*" that is "*reserved to the supplier*". The Vertical Guidelines do not offer guidance as to what is meant with this particular wording. There seems to be a largely shared view that a territory is reserved if it is not allocated to any given distributor ('exclusivity') and if the supplier has made it known to the distribution network that the supplier wishes to keep the territory to itself ('reservation'). The latter point does not imply that the supplier must necessarily be active in the reserved territory. A supplier can also reserve the territory for purposes of a future appointment of a distributor, without commercially developing the territory itself in the meantime.

As the concept of 'supplier' encompasses also all connected undertakings (Article 1(2) of Regulation 330/2010), it is not necessary that the reservation is made by the same legal entity as that which enters into the distribution agreement on the supply-side. This creates room for a scenario where the distribution agreement containing the active sales restriction is entered into by group company A, while the territory to which the active sales restriction is applied is reserved by connected group company B.

A second scenario is that the target territory is an "*exclusive territory*" that is "*allocated by the supplier to another buyer*". The Vertical Guidelines (paragraph 51) make it clear that this implies that the territory must be allocated only to one distributor. Hence, shared exclusivity, whereby the territory is allocated to two or more distributors, is not covered by the exception of Article 4(b)(i) of Regulation 330/2010 (see, paragraphs 0 and following below). The Vertical Guidelines (*ibid*.) make it further clear that the territorial exclusivity (only one distributor) must be contractually guaranteed ("*when the supplier agrees […]*"). Therefore, a purely *de facto* situation of exclusivity (that is not accompanied by any contractual commitment on the part of the supplier) is not sufficient.

There is consensus that the parties to a distribution agreement are free in deciding on the delimitation of the exclusive territories. There is no need or requirement to justify the scope of any such territories. It is our understanding that territories can also be modified over time to accommodate new market situations or, more generally, to match the commercial needs.

According to the Vertical Guidelines (*ibid.*) the concept of exclusive allocation entails an additional requirement (*i.e.*, the parallel imposition of active sales restrictions).

[35] In this respect, the formulation of paragraph 151 of the Vertical Guidelines ("*In an exclusive distribution agreement, the supplier agrees to sell its products to only one distributor for resale in a particular territory. At the same time, the distributor is usually limited in its active selling into other (exclusively allocated) territories […]")* is remarkable as it couples exclusive distribution and the imposition of active sales restrictions, while the logic is that the active sales restrictions are included in the other distribution agreements and are directed at the distribution agreement containing the exclusivity. Hence, unless the whole of the market is covered by exclusive distribution (which in practice is not the norm), it is necessary to distinguish between the agreements that contain the exclusivity (protected agreements) and the agreements that contain the active sales restrictions (the restricted agreements).

Given its major impact on the use of the exception contained in Article 4(b)(i) of Regulation 330/2010, this requirement will be addressed separately below (see, paragraphs 0 and following below).

The same approach is relevant with regard to customer groups. Hence the concepts of reservation and exclusive allocation to one distributor apply *mutatis mutandis.*

2. No passing on of the active sales restriction ('rolling over prohibition')

The second requirement is that the restriction of active sales may not "*limit sales by the customers of the buyer*". The concept of 'customer of the buyer' is defined in Article 1(1)(i) of Regulation 330/2010 as "*an undertaking not party to the agreement which purchases the contract goods or services from a buyer which is party to the agreement*".

This implies that an active sales restriction can be imposed on a 'buyer', but that the restriction cannot be extended (rolled-over) by the supplier to a 'customer of the buyer'. The concept of 'buyer' "*includes*[36] *an undertaking which, under an agreement falling within Article 101(1) of the Treaty, sells goods or services on behalf of another undertaking*". The introductory part of Article 4(b) of Regulation 330/2010 clarifies that "*a buyer party to the agreement*" must be involved.[37]

Article 1(1)(a) of Regulation 330/2010 makes it clear that a vertical agreement covered by the VBER can be entered into "between two or more undertakings each of which operates, for the purposes of the agreement or the concerted practice, at a different level of the production or distribution chain". Hence, it is possible under the VBER to enter into a three-party agreement (supplier – importer – retailer) and to provide that the active sales restriction applies to both the importer and the retailer.

In case the supplier enters into a separate agreement with the importer (the 'buyer'), the retailer qualifies as a 'customer of the buyer' so that it is not possible for the supplier to require from the importer that it imposes an active sales restriction on the retailer in the (separate) agreement with the retailer. The importer can obviously decide to impose such a restriction in its agreement, but it cannot be contractually obliged by the supplier to do so. Otherwise the requirements of Article 4(b)(i) of Regulation 330/2010 are not met.

3. Parallel imposition of active sales restriction

A third requirement to enable an active sales restriction to benefit from the block exemption is that such restriction is imposed on "*all the other buyers of the supplier within the Union, irrespective of sales by the supplier*". This requirement is not explicitly reflected in Article 4(b)(i) of Regulation 330/2010, but is linked in paragraph 51 of the Vertical Guidelines to the notion of 'exclusive allocation'. In our monograph, we have labelled this as the requirement of 'parallel imposition'.[38]

For present purposes, we leave it open whether the Vertical Guidelines actually impose an additional condition or whether they do no more than clarify the notion of 'exclusive allocation' that is included in Article 4(b)(i) of Regulation 330/2010. This

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[36] It is not clear whether the use in this provision of the word "*includes*" (as opposed to "*is defined as*") is deliberate. It is not immediately clear to us which other cases are covered by the concept of 'buyer'.

[37] Article 4(b) of Regulation 330/2010: "*the restriction of the territory into which, or of the customers to whom, a buyer party to the agreement, without prejudice to a restriction on its place of establishment, may sell the contract goods or services […]*" (emphasis added).

[38] F. WIJCKMANS and F. TUYTSCHAEVER, *Vertical Agreements in EU Competition Law*, third edition, Oxford University Press, 2018, pages 216 and following.

issue is however not without importance. In the former case, the requirement of 'parallel imposition' is soft law that binds only the Commission, but not the NCAs or the national courts. In the latter case, the requirement constitutes an integral part of Article 4(b)(i) of Regulation 330/2010 and hence binds also both the NCAs and the national courts.[39]

The parallel imposition requirement has important implications for the supplier from a contractual perspective. It requires that the supplier contractually stipulates an active sales restriction towards the exclusive territory/customer group in the distribution agreements with all of its buyers across the EEA. Without a contractual obligation imposed on the other distributors, it seems impossible for the supplier to ensure that the third condition is met.

It is important to state again that the concepts of 'supplier' and 'buyer' encompass all of the connected undertakings of a given legal entity (Article 1(2) of Regulation 330/2010). This extends obviously the scope of the parallel imposition requirement in cases where different group companies are involved on either side of the vertical agreements applied throughout the EEA.

From the perspective of the supplier there are two aspects that are noteworthy:

- *First*, there is no need to proceed with the parallel imposition of the active sales restrictions when it comes to territories/customer groups reserved for the supplier. The requirement applies exclusively to territories/customer groups allocated to exclusive distributors. Hence, the fact that distributors are at liberty to engage in active selling within a territory/to a customer group reserved to the supplier does not affect the application of the block exemption to active sales restrictions aimed at territories/customer groups exclusively allocated to distributors.
- *Second*, the requirement of parallel imposition does not extend to the supplier. This means that there is no need for the supplier to accept an active sales restriction to territories/customer groups exclusively allocated to distributors. This is a change compared to the VBER's predecessor, Regulation 2790/99.[40] This change brought the VBER more in line with current business practice. It is indeed common that a supplier reserves the right to approach certain types of customers (such as larger accounts for which inter-brand price competition may be more severe) within a territory that is allocated to a single distributor. Such right does not imply that any deal between the exclusive distributor and such customers is excluded. If this customer group is reserved to the supplier, the distributor can be prevented from making active sales, but should remain free to engage in passive sales.

E. Combination exclusive territories/exclusive customer groups

The Vertical Guidelines (paragraph 51) underscore that Article 4(b)(i) of Regulation 330/2010 permits the combination of the allocation of an exclusive territory and an exclusive customer group. In that case, the three cumulative conditions addressed

[39] F. WIJCKMANS and F. TUYTSCHAEVER, *Vertical Agreements in EU Competition Law*, third edition, Oxford University Press, 2018, page 29, paragraphs 1.93-1.94.

[40] See, 2000 Guidelines on Vertical Restraints, paragraph 50: *"[…] A territory or customer group is exclusively allocated when the supplier agrees to sell his product only to one distributor for distribution in a particular territory or to a particular customer group and the exclusive distributor is protected against active selling into his territory or to his customer group by the supplier and all the other buyers of the supplier inside the Community […]"* (emphasis added).

above must be met in respect of both the relevant territory and the relevant customer group.

In practice, the most important point of attention will be to ensure that the parallel imposition is implemented in a manner that considers the two dimensions (territory/customer group). Given that distribution networks are subject to evolution and adaptation, this will most likely require a generally phrased provision that can be supplemented with separate communications to the network spelling out the exclusive set-up (e.g., hotels (customer group) in a given country) that benefits from the active sales restriction that is imposed on the EEA-wide network.

F. Combination of exclusive and selective distribution

From the perspective of active sales restrictions, the Vertical Guidelines offer some guidance on the ability to combine exclusive distribution with selective distribution.

As a general principle, the Vertical Guidelines (paragraph 57) provide that "[w]ithin the territory where the supplier operates selective distribution, this system may not be combined with exclusive distribution as that would lead to a hardcore restriction of active or passive selling by the dealers under Article 4(c) […]". If it is assumed that protection against active sales constitutes an inherent feature of exclusive distribution, this principle is obviously right. In our experience, businesses do however not necessarily associate the need for such protection with the notion of exclusive distribution. The latter notion is typically perceived as a contractual guarantee that the supplier will not designate any other distributor having its location within the exclusive territory (see, paragraph 0 above). The protection against active selling is typically considered a separate feature (additional protection) that can only be granted when specific conditions are met. Exclusive distribution (without this additional feature) is however perfectly achievable in a selective distribution context by operating a system of quantitative selectivity. This position is confirmed in paragraph 152 of the Vertical Guidelines: "A combination of exclusive distribution and selective distribution is only exempted by the Block Exemption Regulation if active selling in other territories is not restricted".

A second combination is that where exclusive distribution is used in certain geographic areas and selective distribution in other areas. A case in point would be that where the supplier applies selective distribution in his home market and adjacent markets where the supplier is successful and has a well-developed network, and exclusive distribution is applied in markets where the supplier's brand name still needs to grow and the overall quality of the network may not meet the same standards. In a very cryptic manner, the Vertical Guidelines (paragraph 56) make it clear that it is possible in such a scenario to impose an active sales restriction on the selective distributors so that the Union-wide parallel imposition of active sales restrictions can be implemented with regard to "*all the other buyers of the suppliers within the Union […]*" (paragraph 51).

There is tension between the (cryptic) language of the Vertical Guidelines and Article 4(c) of Regulation 330/2010. Article 4(c) blacklists "*the restriction of active or passive sales to end users by members of a selective distribution system operating at the retail level of trade […]*". Hence, the blacklisted restriction applies to all members of a selective distribution system and is not geographically limited to the countries or areas where the selective distribution system is applied. The same problem applied with regard to Article 4(b), third indent, of Regulation 2790/99. The language of Article 4(b)(iii) of Regulation 330/2010 has been amended to cure that difficulty and it refers explicitly to "*the territory reserved by the supplier to operate that [i.e., a selective] system*". A similar change was however not made to Article 4(c) of Regulation 330/2010. The combination of the unchanged language of Article 4(c) of Regulation 330/2010 and the cryptic formulation of the Vertical Guidelines (paragraph 56) creates

legal uncertainty. The common understanding is that active sales restrictions can be imposed on selective distributors if that is needed to meet the parallel imposition requirement for all of the EEA. As discussed above, the Vertical Guidelines (paragraph 51) impose the parallel imposition requirement, without differentiating between the distribution systems that the supplier may apply.

A third type of exclusivity/selectivity combination is that where at one level of the distribution chain (e.g., the wholesale level) exclusive distribution is applied and at a different level selective distribution is implemented (e.g., the retail level). The assumption is that at each level the chosen system is applied homogeneously. This particular hypothesis has been raised as an area of concern in the Feedback on the Revision received from some stakeholders. This issue will therefore be further addressed in chapter VII (see, paragraphs 0 and following below, and paragraphs 0 and following below).

VI. Difficulties encountered with the implementation of active sales restrictions

This chapter identifies the most common difficulties encountered in practice with the current VBER regime pertaining to active sales restrictions. While from a purely analytical perspective certain other issues can possibly be raised, the focus of the chapter is on the matters reported to us by the Contributing Practitioners and is based on our own experience in dealing with client demands.

A. Need for more guidance

Generally speaking, the text of the VBER and the Vertical Guidelines is considered by businesses and their advisors to be very technical. This observation applies in particular to the conditions governing active sales restrictions.

The feedback that we have received from the Contributing Practitioners is that in many jurisdictions businesses face difficulties with the interpretation and application of the technical rules of the VBER (see, paragraph 0 above). The Vertical Guidelines do offer useful guidance on how to interpret and apply the VBER in respect of active sales restrictions, but remain very cryptic for individuals without much expertise in the field of assessing vertical agreements and without access to relevant (often international) publications.

A striking example provided by one of the Contributing Practitioners was that in its jurisdiction it is still very common to appoint exclusive distributors and to impose in the same distribution agreement a complete prohibition on active sales outside the exclusive distributor's territory (*i.e.*, the old Regulation 1983/83 regime). In the manner in which the prohibition was formulated no account is taken of the characteristics of the target territories that are protected by the prohibition and whether such territories are exclusively allocated (see, paragraph 0 above) This observation is consistent with what we see in our own practice. We still encounter exclusive distribution agreements that do not comply with the most basic requirements set by the VBER. This is clearly not deliberate as other sections of the agreements (such as the fixed term linked to the non-compete obligation) demonstrate that efforts are made to meet the requirements of the block exemption and thus the problem seems to stem from a lack of understanding of the rules on active sales restrictions.

We do not believe that the VBER and the Vertical Guidelines can be blamed for such very basic mistakes. By the same token, it is undeniable and confirmed by the Contributing Practitioners that the more detailed aspects of the current regime on active sales restrictions are difficult to capture based on the text of the VBER and the Vertical Guidelines. For example, the parallel imposition requirement, which has severe consequences when setting up and managing an active sales regime, follows from one simple phrase in the Vertical Guidelines, without much further explanation: "*the exclusive distributor is protected against active selling into its territory or to a particular customer group by all the other buyers of the supplier within the Union*" (paragraph 51). There is no mention of this requirement in the text of the VBER. In addition, businesses need to understand that the parallel imposition requirement does not apply to the supplier from the mere reference to "*irrespective of sales of the supplier*". Similarly, the fact that the parallel imposition requirement does not apply to territories or customer groups reserved by the supplier to itself is not mentioned explicitly and must be inferred from the absence of any reference in the texts to that effect. The available guidance is for non-experts (which represent the majority of practitioners dealing with distribution agreements and their assessment under the VBER) too limited to be able to capture all these legal nuances. However, given that

active sales restrictions are to be situated in a hardcore environment, the failure to do so has significant legal consequences.

The Vertical Guidelines explain that the Commission "*aims to help companies conduct their own assessment of vertical agreements under EU competition rules*" both under the VBER and outside the scope of the VBER. The Vertical Guidelines address the assessment in individual cases quite extensively. However, in our experience businesses and their advisors are rather reluctant to conduct a complex individual self-assessment on the basis of Article 101(3) TFEU and the guidance provided in paragraphs 96 and following of the Vertical Guidelines. In our practice we have conducted over the past 10 years one (1) full-blown autonomous self-assessment of a pan-European distribution network on the basis of the conditions of Article 101(3) TFEU and the guidance offered by the Vertical Guidelines. The vast majority of the Contributing Practitioners have confirmed not to have engaged in any such substantive self-assessment exercise.

The standard practice for cases falling outside the scope of application of the VBER – for example because the market shares exceed to a certain extent the limit of 30% or for other technical reasons – is to rely upon the VBER "*by analogy*". This offers businesses the certainty that when the distribution agreement is challenged for enforceability reasons, it does not contain hardcore restrictions and no negative presumption applies. As a consequence of this practice, the impact of the VBER extends in reality beyond its actual scope of application and is of practical relevance also for agreements that are technically not covered by it as it provides more legal certainty than undertaking an individual self-assessment.

The foregoing implies that, for most of the practitioners, the initial 73 paragraphs of the Vertical Guidelines are of the greatest practical relevance. These paragraphs serve as the primary source for understanding the legal requirements underpinning the VBER.

Based on the input received from the Contributing Practitioners and our own experience in discussing the requirements of the VBER with businesses and their legal departments, compliance with the requirements of the VBER and legal certainty would be greatly enhanced if the Vertical Guidelines, when addressing active sales restrictions, are expanded considerably and are phrased in such terms (possibly accompanied by examples) that the common users of this legal instrument grasp more readily what is needed to avoid hardcore problems on account of the application of an incorrect active sales regime.

B. Evolution of the network

Business reality shows that a supplier's needs in respect of its distribution network evolve over time. A business will often start in a single market or a limited number of markets with a non-exclusive/non-selective distribution set-up. At a later stage when the business has grown, its activities may expand into other markets or it may be in a position to add more qualified distributors in its existing markets or even to replace the existing distributors by new and better ones.

As confirmed by several Contributing Practitioners, practice shows that the current regime applicable to active sales restrictions would not seem to take full account of the business reality of evolving distribution networks:

1. No coverage of the whole of the EEA

A first issue is that a great number of businesses that apply the VBER are not necessarily active throughout the whole of the EEA. This is a reality that we have encountered frequently in our own practice.

One of the Contributing Practitioners provided the following striking example. A supplier of branded clothes had appointed exclusive distributors in three national markets and reserved two national markets for itself. The supplier had decided not (yet) to enter other national markets and considered these five markets as the (then) natural perimeter of its activities. The agreements were drafted correctly and provided for active sales restrictions in a correct manner. The agreements did however not address the other national markets which were not reserved to the supplier nor allocated to any exclusive distributor. Very soon, the supplier's clothes were being sold in other national markets by at least one of the three exclusive distributors. As such, the fact that the supplier did not immediately reflect upon a distribution strategy covering the entire EEA caused difficulties. The supplier was in practice no longer in a position to reserve these other markets and was likewise unable to offer a newly appointed exclusive distributor in any of these markets protection against active sales. Such protection would require negotiating additional restrictions for the existing exclusive distributors. The existing distributors had, however, no incentive to accept a change to their agreements that would limit their scope of activity, even though their acceptance is needed to meet the parallel imposition requirement. The protection against active sales restrictions could therefore no longer be validly included in the distribution agreements of any newly appointed exclusive distributors in those territories by the supplier.

This example underscores two practical difficulties:

- Companies that do not have (at least initially) pan-European ambitions risk to face difficulties if they do not design and set up their network from the outset on a pan-European basis (e.g., by reserving all of the EEA countries in which no distributor is appointed). This is obviously not an immediate result of the current block exemption regime, but results from a lack of understanding of the regime (and in particular the parallel imposition requirement) at an early stage of the roll-out of the distribution network.
- If the supplier has started to roll out its network and failed to introduce active sales restrictions in the agreements with the initial distributors, it will no longer be in a position to insert active sales restrictions in any subsequent distribution agreements. The incumbent distributors have no incentive to accept any such restrictions. This triggers a spill-over effect, notably that due to the parallel imposition requirement it will not be possible to insert active sales restrictions, even just in the newly concluded distribution agreements.

2. Transition difficulties

Even if the distribution network of a supplier covers the whole of the EEA, it does not match with the business reality in a vast number of cases that the relevant agreements have been concluded with similar terms and conditions more or less in the same time frame. The reality is that networks do not only grow geographically (see, previous point), but also in terms of the substantive aspects of their set-up. This point has been highlighted by several of the Contributing Practitioners.

The conditions on the basis of which active sales restrictions can be imposed under the VBER do however not take this business reality into account. They seem to assume that the supplier is in a position to set up his exclusive distribution network from scratch and can easily amend the contractual arrangements with all distributors throughout its entire network. Such assumption is however not correct. A distributor may not (always) have an interest in accepting a change, even if the supplier is prepared to compensate the distributor for the loss of opportunities. It would likewise be incorrect to assume that suppliers operate exclusive distribution set-ups covering the whole of the EEA. The reality is that most non-selective networks consist of a

mixture of scenarios where exclusive set-ups are combined with non-exclusive arrangements in other territories.[41]

Typical cases that we have encountered in our practice include scenarios where the supplier initially operated in a given territory with a number of non-exclusive distributors. Based on experience it becomes clear that one of the distributors stands out and is prepared to devote more attention and financial resources to the development of the brand. The supplier is prepared to terminate the other distributors in the territory and to promote that preferred distributor to an exclusive status. An alternative scenario that we have encountered is that where the supplier wishes to preserve all of the distributors, but intends to grant exclusive distribution rights in a defined part of the territory to one of them on account of its performance and willingness to invest in that area.

The creation of territorial exclusivity will in both these scenarios not present a problem. The transition from non-exclusivity to exclusivity (*i.e.*, a contractual guarantee that no other distributors will be appointed within the designated territory) is a matter that is under the complete control of the supplier and the relevant distributor. The problem is the introduction of active sales protection to the benefit of the distributor. In this respect practice shows that there are difficulties at two levels:

- Unless the supplier has introduced from the outset in all of its existing distribution agreements a generically phrased active sales restriction[42] (which, in our experience, would not necessarily be the case), it will need to convince all of the other distributors to amend their agreement and to introduce an active sales restriction. This obviously causes major issues in practice. There will not necessarily be an incentive for the other distributors to renegotiate the agreement, and even less so to accept an active sales restriction towards other territories/customers. During the negotiations of a distribution agreement, exclusivity is often seen as a reward for the distributor in return for its commitment to focus its efforts on a given territory/customer group. In return for the assurance that no other distributors will be appointed within its territory/towards its customer group, a distributor is under such circumstances more willing to accept an active sales restriction towards other territories/customers. The same incentive or business interest is lacking, where a supplier is required to renegotiate the agreement merely for purposes of imposing an additional sales restriction that operates to the benefit of other distributors and for which it receives nothing in return. The argument that acceptance of this amendment is needed to ensure compliance with a formal condition under the VBER will not carry much weight in these negotiations.
- A second issue arises where the supplier that wishes to grant exclusivity combined with active sales protection is a local subsidiary within a larger group, having no relationship with distributors in other markets which are the responsibility of the other local subsidiaries of the group. The current conditions require that the local subsidiary aligns with other local subsidiaries or with the HQ-level for purposes of causing all of the distribution agreements to be amended. This will include for the most part agreements to which the local subsidiary is not even a party and over which it has no control. The local subsidiaries have no means of imposing the active sales restriction on distributors with which they have no contractual relationship. Other local subsidiaries or HQ lack in most of the cases the business interest

[41] See, in this respect, again the remark in footnote 35 above.

[42] For an example, see, paragraph 0.

to facilitate such a change. One of the Contributing Practitioners mentioned that, in a case encountered in its practice, the lack of similarity of the distribution systems used in different Member States rendered such discussions simply impossible. In such instances and given the parallel imposition requirement, a local supplier is practically not in a position to offer its newly designated exclusive distributor any protection against active sales by other buyers.

Under the current regime, as soon as the active sales restriction is not imposed contractually on all the other buyers of the supplier from the outset, the supplier will face major difficulties to remedy the situation subsequently and to introduce protection against active sales for newly appointed distributors or distributors that are converted to an exclusive status.

All of this goes to demonstrate that the existing block exemption regime regarding active sales restrictions makes it difficult (and often impossible) to introduce this type of protection when distribution networks evolve and the need to offer such protection becomes relevant from a business and economic perspective. In practice and as soon as the VBER requirements have been properly understood by the business, the imposition of active sales restrictions as a tool to protect investments becomes highly unattractive and a switch to selective distribution is often considered more realistic.[43]

In the case of a switch to selective distribution, there is an incentive for every distributor to accept the new concept as all distributors can gain from the switch. The position is different for exclusive distribution, unless the supplier decides to convert all of its distributors to an exclusive status. In a case that we encountered in our practice, the latter option was applied as the switch to selectivity did no really make business sense. Exclusive distribution was offered to all of the distributors in order to have a negotiation argument to cause the distributors to accept the active sales restriction. Exclusivity was granted to distributors that would otherwise never have been offered this possibility. The supplier tried to keep the situation under control by limiting the scope of the contract territories to a minimum for those distributors that were given exclusivity solely for negotiation purposes and to ensure that the parallel imposition requirement could thus in practice be met.

C. Shared exclusivity

It is our understanding that the need for more flexibility as to shared exclusivity has been brought up by stakeholders during the evaluation of the current VBER regime.[44]

Shared exclusivity is not eligible for protection against active selling under the VBER. An active sales restriction can only be imposed within a territory/towards a customer group that has been exclusively allocated to one single distributor/reserved for the supplier. Active sales restrictions in a territory where two or more non-exclusive distributors are active, are thus not allowed. Active sales restrictions are currently also not possible when two or more distributors received a contractual guarantee that no other distributors will be appointed.

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[43] Our practice seems to be confirmed by the findings of the evaluation study, as it was found that "*exclusive distribution is not a widespread practice, with only a limited number of stakeholders reporting the use of this distribution model. The market investigation performed as part of the evaluation study indicated that selective distribution is generally preferred over exclusive distribution, as it allows to achieve the same benefits while reducing costs and allowing better market coverage*". See, Commission Staff Working Document on the Evaluation of the VBER, page 189.

[44] Commission Staff Working Document on the Evaluation of the VBER, pages 141 and 190.

Our own practice and the input received from the Contributing Practitioners underscores that the current regime lacks flexibility in this respect and, on account hereof, may lead to undesired results.

A striking example from our own practice is a case where a supplier had seven non-exclusive distributors and wished to keep a direct relationship with the three most successful distributors. In order to motivate these distributors to focus their sales efforts within a specific territory (a metropolitan area), the supplier was willing to guarantee each of them that no additional distributors would be appointed and to offer each of them protection against active sales restrictions by other distributors.

The key issue was that all three of the distributors wished to remain active in the whole of the metropolitan area in which they were located and to be acknowledged (marketing wise) as distributors for that entire metropolitan area. This approach was entirely consistent with the wishes of the supplier, which in fact saw benefit in the three distributors actively competing with each other in the metropolitan area. Due to the constraints imposed by the VBER, a choice had to be made between receiving no protection against active sales coming from distributors situated outside of the metropolitan area or carving up the metropolitan area into separate exclusive territories and each of the distributors accepting an active sales restriction towards each other's territory. The choice was then made to go for the protection against active selling and thus to carve up the metropolitan area. However, there was no real business need for doing so and, from a competition law perspective, it had a more far-reaching impact than needed. The business concern would also have been met if shared exclusivity would have allowed the imposition of active sales restrictions. In such case, the three distributors are appointed as distributors for the whole of the metropolitan area, receive the contractual guarantee that no other distributors will be appointed and, in addition, they benefit from protection against active sales by the other buyers of the supplier. By the same token, competition (both active and passive) between the three distributors within the metropolitan area would have been preserved. Hence, for formal compliance reasons the scheme that was adopted restricted competition more than was needed for business and economic reasons.

Another example where a more flexible approach (shared exclusivity) would have allowed to meet a supplier's business needs, relates to the sector for out-of-home ice cream. This case was brought to our attention by one of the Contributing Practitioners. The supplier had divided its country in regional areas with regional distributors focusing their efforts and investments on their specific region. None of these regional distributors was (technically) able to cover the entire national market. In addition, the supplier had also a relationship with one larger distributor who was in a position to cover the entire national market for a wider range of frozen food products (including out-of-home ice cream). The supplier needed the relationship with the larger distributor to ensure complete coverage of the country. Given that there was overlap between the territories and customers covered by the regional distributors and the larger national distributor, the supplier was unable to appoint exclusive distributors and to offer protection against active sales. Such protection would however have been desirable given the local investments made by each of the regional distributors. If shared exclusivity would have been allowed between the regional distributors and the national distributor, it would have been possible for the supplier to introduce protection against active sales in order to motivate the regional distributors to make the additional efforts and investments.

A third example that was mentioned by one of the Contributing Practitioners concerns the sector of home furnishing. A supplier chose a non-exclusive/non-selective distribution model to distribute its products in different EEA countries. Different distributors were present within the same territory and the requirements contractually imposed differed from country to country. In country A the supplier sold products to a

purchasing group which, on account of the purchase volumes, obtained lower prices. Some members of the purchasing group started to sell the products actively in country B, offering much lower prices than the local distributors. However, the requirements imposed on the distributors in country B were substantially higher than those applicable to the distributors in country A. As a result, the supplier came under pressure as the distributors in country B questioned their willingness to continue with their efforts and investments. In order to solve the situation, the supplier carved up country B in exclusive territories and imposed active sales restrictions in order to protect the efforts and investments in country B. However, also in this case the supplier would have preferred to implement a form of shared exclusivity across country B, without the need to artificially divide the country in exclusive territories.

In all scenarios, the impact on (intra-brand) competition of shared exclusivity (instead of single exclusivity) would have been less, as the (shared) exclusive distributors would have continued to compete with one another in the same territory. The option to allow for more flexibility in this respect is addressed below in paragraphs 0-0 below.

D. Parallel imposition requirement

Our advisory practice and the feedback we received from the Contributing Practitioners shows that the parallel imposition requirement (see, paragraphs 0-0 above) is seldom correctly understood by businesses and, when understood, it is perceived as a major practical and legal obstacle. Furthermore, when discussing this requirement with clients, there is genuine disbelief that the failure to include an active sales restriction in a Maltese distribution agreement may trigger a hardcore problem for an active sales restriction included in a Swedish distribution agreement of which the enforcement is sought based on active sales made by the Swedish distributor into an exclusive territory located in Finland.

Several Contributing Practitioners have confirmed that the parallel imposition requirement is the single most important reason why they have stopped advising the use of active sales restrictions. A Contributing Practitioner confirmed that, on account of legal uncertainty, it systematically causes active sales restrictions to be removed and replaced by location clauses. Another Contributing Practitioner confirmed that the considerable shift towards selective distribution can in part be explained by the difficulties to adhere to the parallel imposition requirement, which renders exclusive distribution coupled with active sales protection very unattractive.[45]

Unless the distribution network is extremely stable and consists of a very limited number of distributors across the EEA, it seems nearly impossible to draft an active sales restriction that is tailored towards the actual business needs and is not phrased in very general terms. An example of such a generally phrased active sales restriction is the following: "*The [buyer] will exercise its activities within [the territories]. The [buyer] shall not engage in active sales in territories which are exclusively reserved for the [supplier], nor in any territory exclusively allocated to another buyer appointed by the supplier*". In our practice, even networks consisting of a single country-wide distributor resort to such a generally formulated active sales restriction to avoid enforceability risks. In any event, given the risk presented by the failure to meet the parallel imposition requirement, we have not advised over the past years to include any active sales restriction that is formulated more specifically than the general clause cited above.

[45] See, in this respect, also paragraph 0, *in fine*, above.

There is however at least a double problem with a generally formulated active sales restriction:

- It goes further than is actually needed to protect investments made by certain distributors by extending the application to all exclusive distributors. As mentioned above (see, paragraph 0 above), the exclusive appointment by a supplier of a distributor does not always need to coincide with the protection against active sales by all other distributors in its territory.
- It creates uncertainty as to its scope of application and risks to boil down to a general restriction of active sales outside the territory of the exclusive distributor. Distributors will typically not know which territories are reserved or exclusively allocated to another distributor. Hence, the effect of the provision is to place us back in a Regulation 1983/83 scenario where the exclusive distributor is inclined not to engage in any active selling outside its own exclusive territory.

The practice of the Contributing Practitioners and also our own practice show that, very often, a supplier is not aware that it is only able to offer a distributor active sales protection when it has foreseen a corresponding obligation within the contractual relationships with all of its other distributors (see, paragraph 0 above). Even where they are aware that there is a requirement of this nature, they often believe that it is sufficient to include the restriction in their own distribution agreements, but fail to acknowledge that the restriction must also be included in the distribution agreements concluded by all of the other group companies within the EEA.

The lack of an explicit contractual obligation imposed on "*the other buyers*" to refrain from engaging in active sales in a given exclusive territory is a cause for legal disputes and legal uncertainty.

A first example where the parallel imposition requirement has been a cause for legal dispute relates to the food retail sector. A producer of food products appointed an exclusive wholesaler for the distribution in country A. The producer agreed not to sell any products to other buyers in country A. In country B, the producer sells directly to different retailers. A retailer which is active in both country A and country B, and which purchases the products directly from the producer, also started selling them in its retail outlets in country A. The producer did not impose an active sales restriction towards country A in its agreement with the retailer located in country B. As such, there was no contractual obligation for the retailer that prevents it from selling in country A. Nevertheless, the retailer was summoned by the wholesaler located in country A on account of the former's role (alleged complicity) in causing the producer not to prevent the retailer in country B from engaging in active sales in country A. The difficulty with this matter is that the active sales restriction was not even included in the agreement with the retailer located in country B, let it be that it was picked up in all of the other distribution agreements entered into by the producer. As such, the retailer in country B was not contractually restricted from selling actively in country A. The claim by the wholesaler seems therefore to be based on the assumption that exclusivity automatically and even tacitly includes protection against active sales. The wholesaler seems to ignore that the parallel imposition requirement can only be met by inserting the relevant contract language in all of the distribution agreements of the supplier covering part of the EEA.

Another case reported by one of the Contributing Practitioners equally relates to the food retail sector. In this case, it was the supplier who wished to prevent a wholesaler from selling in a territory on the basis of an active sales restriction, even though such a restriction was not foreseen in the contractual arrangements. The supplier argued that it could legitimately enforce an active sales restriction based upon Article 4(b)(i) of Regulation 330/2010, without the need to include a provision to that effect in its

agreements. The wholesaler replied that the parallel imposition requirement for imposing an active sales restriction was not met automatically due to the operation of the VBER, that it necessitated contractual provisions in the various distribution agreements and therefore that no active sales restriction could be enforced against it.

These cases reflect a rather fundamental misunderstanding of the practical and legal implications of the parallel imposition requirement. The fact that an active sales restriction may benefit from an exemption from a competition law perspective, does not mean that such restriction is automatically applicable between the parties to an exclusive distribution agreement. The same observation applies to any suggestion that active sales restrictions are automatically included in non-exclusive distribution agreements towards reserved or exclusively allocated territories. The imposition of active sales restrictions requires first a contractual arrangement to that effect. The issue of the compatibility with the VBER (and hence the enforceability of the active sales restriction on that basis) comes up only in a subsequent step. This second step will imply, on account of the parallel imposition requirement, that all of the distribution agreements across the EEA contain the appropriate active sales restrictions.

It is fair to conclude, based on our own practice and the input provided by the Contributing Practitioners, that the parallel imposition requirement is the single most important difficulty encountered by businesses and their advisors with the current regime on active sales restrictions.

E. Rolling over prohibition

The second condition for imposing an active sales restriction is that it may not "*limit sales by the customers of the buyer*" (see, paragraphs 0-0 above). A customer of the buyer can thus not be prevented from selling where or to whom it wants. This implies furthermore that an active sales restriction cannot be rolled-over downstream by contractually obliging an independent importer or independent distributor to include the same active sales restriction in its own downstream distribution or supply agreements.[46]

In practice, this requirement is a cause of concern as it means that the level of protection that can be offered arbitrarily depends on the extent to which the supplier is vertically integrated.

- A supplier with integrated importing companies appoints independent distributors at the retail level and will therefore be able to protect the retail level against active sales by other independent distributors appointed by the supplier. However, where a supplier operates with independent importers, which in turn appoint distributors at the retail level, the restriction will only apply at the importer level, but the distributors appointed by the independent importer cannot be prevented from engaging in active sales in other exclusive territories. Hence, the level of integration has a direct impact on the degree of protection against active sales that can be implemented.
- In addition, the extent to which a supplier is vertically integrated may differ across the EEA. In our practice and even when dealing with large multinational groups, we see that importers are not always integrated companies and that in certain jurisdictions (in our practice often Greece and Portugal) independent importers are appointed. Due to the rolling over prohibition this results in a somewhat awkward mix of active sales

[46] The 'rolling over prohibition' was also identified as an issue regarding exclusive distribution during the evaluation. See, Commission Staff Working Document on the Evaluation of the VBER, page 83.

restrictions. In the more integrated countries (A) the first independent buyers are situated at the retail level and these buyers can be prevented from engaging in active selling. In the less integrated countries (B), the active sales restrictions can only be imposed at the importer level and the supplier cannot require that the importer includes a corresponding restriction in the agreements with its distributors. Practically speaking, this means that a retailer located in country A can be prevented from making active sales in an exclusive territory of a retailer in country B, but that the same retailer situated in country B cannot be prevented from making active sales in the exclusive territory of a retailer in country A.

We were informed by one of the Contributing Practitioners about the following business example concerning the distribution set-up of a supplier of branded clothes that illustrates this problem perfectly well. The supplier was present in different territories and acted in each of these territories either

- as exclusive general importer and wholesaler/retailer;
- as exclusive general importer selling to an exclusive independent wholesaler;
- as the supplier of an exclusive independent importer/wholesaler;
- as the supplier of an exclusive independent importer/non-exclusive wholesaler;
- as the supplier of an exclusive independent importer.

Due to the prohibition to pass on the active sales restriction, it becomes in such a complex setting highly arbitrary at what trade level protection against active selling can be secured.

A possible solution that we have advanced in our monograph is for the supplier to conclude a three (or multi) party agreement. The rolling over prohibition applies in relation to a 'customer of the buyer', who is defined in Article 1(1)(i) of Regulation 330/2010 as "*an undertaking not party to the agreement*". It follows from this definition that, when a customer acting at a different level of trade becomes a party to the same agreement, an active sales restriction can be imposed and hence be rolled over (see also, paragraph 0 above). Such a solution (apart from being very formalistic) is only workable in very specific circumstances. Often a supplier has no (and does not want to have a) direct relationship with the distributors of his importer/wholesaler or the importer/wholesaler is not prepared to facilitate such a multiparty agreement so as to remain the single contractual point of contact for its network.

Several Contributing Practitioners have emphasized that, together with the parallel imposition requirement, the rolling over prohibition is one of the main reasons for not advising a system of exclusive distribution coupled with protection against active sales. When properly understood and devised, a system of quantitative selective distribution (which can include location clauses) provides much more legal certainty and can offer protection of investments that is the same or even better than what is offered by a system of exclusive distribution (see, paragraphs 0-0 above). It is important to acknowledge that, with the exception of the protection against active selling, a system of quantitative selectivity can provide all the protective features of exclusive distribution.[47] The difficulties related to the parallel imposition requirement

[47] In order to roll out a comprehensive selective distribution network it is furthermore not necessary to engage in multiparty agreements covering different levels of trade. It is perfectly

and the rolling over prohibition make the use of active sales restrictions risky. Any mistake puts the entire agreement outside the VBER and taints the set up with a hardcore problem.

F. Difficulties encountered in hybrid situations

A hybrid scenario concerns the situation where the supplier combines different distribution set-ups (see, paragraph 0 above).

A first such scenario is that where selectivity is applied in certain territories, exclusivity in other and non-exclusive/non-selective still in other territories. Such a situation may correspond to genuine business needs. For instance, in many cases there is not (yet) an immediate business need for the supplier to directly implement a selective system covering the entire EEA and it makes sense, particularly in newer markets, to operate first a non-exclusive/non-selective system.

A second hybrid scenario concerns the situation where exclusivity and selectivity are combined at different trade levels. This is the case where an exclusive importer/wholesaler is appointed, which is responsible for developing a selective network of retailers. This scenario is addressed in paragraph 63 of the Vertical Guidelines.

A third hybrid scenario is that where the supplier has split its product offering and links the different offerings to different distribution systems. Classic cases that we have encountered in our practice include a split between innovative household appliances (for which selectivity is used) and more commodity-like appliances (non-exclusive distribution) and a split between heavy motorcycles (selectivity) and other motorcycles and mopeds (exclusivity). This third scenario does not warrant a separate discussion as it functions well within the framework of the VBER.

The difficulties encountered by businesses in respect of hybrid scenarios are different when it concerns a territorial hybrid scenario (first scenario) or the combination of exclusivity and selectivity at different trade levels (second scenario). We will therefore discuss both scenarios separately.

1. Territorial hybrid scenarios

In a territorial hybrid scenario, the difficulties are one-directional and concern essentially the territories where selective distribution is applied. This is so because, where exclusivity and selectivity are combined, the exclusive distributors can be protected in their territories against active sales from non-exclusive and/or selective distributors. Despite the general rule that selective distributors cannot be subjected to any active or passive sales restrictions of a territorial nature (Article 4(c) of Regulation 330/2010), the Vertical Guidelines (paragraph 56)[48] stipulate an exception where active sales restrictions are imposed on selective distributors towards exclusively allocated territories or customers. Hence, the fact that selective distribution is applied in certain territories does not affect the protection against active sales that can be offered to exclusive distributors situated in other territories.

However, selective distributors do not benefit from a similar protection in the opposite direction. This may damage the efficient functioning of a selective distribution network. Selectivity ensures that products are supplied by a closed network of distributors, which each meet the appropriate quality standards. Under the current

compatible with the VBER that a manufacturer imposes on its importer a contractual obligation to implement a selective distribution system at the retail level.

[48] Paragraph 56 of the Vertical Guidelines is not explicit as to whether this possibility can be extended to territories reserved to the supplier.

VBER regime, non-selective distributors located in non-selective territories cannot be prevented from selling to non-authorized distributors in territories reserved to operate the selective system. This may undermine the entire selective distribution set-up. Selective distributors which undertook (serious) efforts to meet the quality standards risk to be confronted with sales by unauthorized distributors, who are not subject to the same requirements.

In our practice this risk has had a major impact on the implementation of transition scenarios where a supplier moves from a non-selective system to a selective system. In most cases the wish to move towards selective distribution concerns only a limited number of countries. A good example from our practice concerns the distribution of architectural lighting equipment. The producer of the equipment was well-established in a number of countries and it had identified suitable distribution channels to take the distribution to a next level. When properly explained, the relevant distributors understood the selective distribution concept and were prepared to make extra investments in return for the protection against free riding offered by selectivity.

There were mainly two reasons why the supplier preferred not to roll out selective distribution immediately to all countries of the EEA. The first had to do with purely practical considerations. The transition from non-selectivity to selectivity requires careful explanation to the network and involves a considerable administrative burden (with new agreements that need to be signed more or less simultaneously). For most organizations, it is not workable to do so in multiple countries within a relatively short time span. The second reason was that in certain markets the right distributors had not yet been identified and those that were suitable were not yet in a position to accept the quality requirements (and related investments) applicable in the selective countries.

In the strategic assessment of the transition, the inability to impose a selectivity requirement (prohibition to sell to unauthorized distributors in selective territories) was perceived as a major risk. In the core territories that were selected for implementing a selective distribution network there were existing distributors that might not be willing to accept the new quality requirements and the related investments. Those distributors would have to be terminated, but would be looking for alternative sourcing opportunities. The non-selective territories present such opportunities. The same applies to traders that were not in direct contact with the supplier, but had been sourcing from the existing distributors. Those traders will not become part of the selective network and can therefore no longer be supplied by the distributors in the selective territories. Also those traders would be looking for alternative sourcing possibilities. The concern was that, if such alternative sourcing would work, the distributors that have made the necessary investments to become part of the newly established selective network would be discouraged and believe that the supplier had not done everything within its power to secure the protection of their investments.

In our practice, we advise increasingly not to go for a gradual geographic roll-out of a new selective distribution system, but to do so more or less simultaneously across the whole of the EEA ('Big Bang' implementation). In order to render this scenario workable, the countries that are not high on the priority list are given a very short and basic selective agreement containing limited requirements that necessitate hardly any real investments. In this manner the investments in the core countries can be protected on the basis of a selectivity concept that applies across the EEA.

A second example relates to the sector of kitchen equipment. A supplier of kitchen equipment distributed its products mainly in five or six core (national) markets. A distinction was furthermore made between the standard product offering, distributed through non-exclusive/non-selective distributors and the high-end premium products,

distributed via a selective network in the core markets. The supplier was however not yet in a position to implement a selective network throughout the EEA, as it still lacked presence in certain markets or its business was not yet sufficiently developed in other markets. On an *ad hoc* basis, the manufacturer delivered its non-premium products also outside the core markets. However, in order to avoid the risk that unauthorized distributors start selling also its premium products from outside the core markets to non-selective distributors within the core markets (*i.e.*, the selective territory), the manufacturer did not sell such premium products in territories outside the selective network. The premium products were exclusively reserved for the selective territory. If there is not a major risk that such sales may undermine his selective network, the manufacturer would most likely have seized the opportunity to develop the sales of its premium products also in other non-core markets.

These two examples taken from our own practice underscore how the current VBER regime, either causes suppliers to opt for a more restrictive distribution set-up (selectivity across the EEA as opposed to a hybrid scenario) in respect of which they are certain to benefit from the block exemption, or to be reluctant to bring certain products to new markets where selectivity is not applied.

2. Combination of exclusivity/selectivity at different trade levels

Generally, the combination of exclusivity and selectivity at different trade levels is not possible. This follows from the requirement that within a selective distribution network, cross supplies between distributors, "*including between distributors operating at different level of trade*" cannot be restricted (Article 4(d) of Regulation 330/2010).

One of the Contributing Practitioners shared an example from his practice where the VBER regime was deemed problematic. The case concerned a manufacturer of highly specialized IT hardware and software that is used by businesses and organizations. The supplier adopted a distribution model throughout Europe consisting of a single distributor per country at the wholesale level, which in turn designates and administers several selective retailers. The distributor cooperates closely with the manufacturer and is expected to make special efforts and investments to support the retailer network. In order to motivate the distributor to assume this role, the manufacturer wished to (i) restrict active sales between different countries at the wholesale level (*i.e.*, preventing the distributor in country A from actively approaching the retailers in country B) and (ii) restrict sales to unauthorized traders. While the second aspect (ii) is feasible under the VBER, the first (i) is not. The business aspirations of the manufacturer were therefore only partially implemented.

By way of exception, the Vertical Guidelines refer in paragraph 63 to a very specific hybrid scenario, which may in individual cases fulfil the conditions of Article 101(3) TFEU. It concerns the scenario where wholesalers are appointed in different territories and are required to invest in promotional activities in their territories in support of the sales of their authorized retailers, but where it would not be practical to specify in a contract the required promotional activities. In such a case, the Vertical Guidelines explain that an active sales restriction may be imposed on the wholesalers preventing them from selling actively to selective retailers located in another wholesaler's territory.

In our experience, the hypothesis described in this specific paragraph of the Vertical Guidelines is mainly theoretical and lacks practical relevance.[49] We, nor the

[49] Our practical experience in this respect would not seem entirely in line with the experience mentioned by certain stakeholders, as explained in the Commission Staff Working Document on

Contributing Practitioners have come across an example, where a business felt sufficiently comfortable that its distribution set-up fell within the scope of paragraph 63 and could therefore benefit from an individual exemption. Even if that were the case, the consequences of applying paragraph 63 are unhelpful.

There are multiple reasons that may explain why the exception contained in paragraph 63 does not work in practice. First, the condition that "*it is not practical to specify in a contract the required promotional activities*" triggers substantial uncertainty. In our experience, we fail to see the case where a supplier would have sufficient certainty that this condition is met and cannot be disputed. A second reason is that the exception is not covered by the VBER. Given that paragraph 63 refers to an individual exemption and not to the inapplicability of Article 101(1) TFEU, the active sales restriction qualifies in any event as a hardcore restriction. Even if the conditions for an individual exemption are met, the entire distribution agreement still forfeits the benefit of the block exemption. This is a completely unattractive prospect.

G. Customer-oriented channel management

Under the current VBER regime, it has proven impossible, or at least difficult for a supplier to organize his distribution network by implementing a customer-oriented approach or engage in customer-oriented channel management.

This concerns the scenario where a supplier wishes to appoint a distributor which focuses on, and specializes in a specific customer channel. Specific customer channels may necessitate different expertise and different distribution strategies, requiring different investment efforts. For certain products it may make sense to distinguish between distributors focusing their efforts on specific channels. Examples provided by the Contributing Practitioners include the need for separate channels for animal as opposed to human pharma, pharmacies as opposed to hospitals, horeca as opposed to retail and B2B customers as opposed to B2C customers. Customer-oriented channel management may be expected to be beneficial for customers, as the customers will benefit from pre-sales services (based on experience with the channel) and corresponding investments that are better targeted to their specific situation and needs.

However, the VBER does not facilitate a distribution set-up enabling genuine customer-oriented channel management. The main obstacles result from the rolling over prohibition and the fact that passive sales always remain possible. As a result of these obstacles, a supplier will not be able to provide assurances to a specialized distribution channel that it will not be confronted with sales by other distributors of the supplier (or their customers) which are free riding on the efforts and investments of the specialized distributor in its customer channel. Particularly smaller suppliers may face difficulties to convince a channel specialist to take under these conditions their products or services on board.

From a policy perspective there is obviously a balancing act to be performed between, on the one hand, facilitating access to channel specialists (by offering protection against freeriding) and offering customers their expertise and services and, on the other, avoiding the risk that such channel management leads to a silo approach that facilitates price discrimination to the detriment of customers. The current VBER regime seems to give more weight to the second aspect than to the first as it limits the ability to protect channel specialists (only) to the first tier imposition of active sales

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the Evaluation of the VBER, pages 83, 140 and 191. This may follow from the fact that a hybrid set-up at different trade levels is highly uncertain under the current VBER regime and that we therefore steer businesses away systematically from such a hybrid set-up. We do indeed fail to see how such hybrid set-up can be implemented without triggering genuine compliance risks.

restrictions directed at a specified customer group (possibly linked with territorial exclusivity). When explaining this limited possibility to the business, the general conclusion is that it does not really promote channel management and the protection of channel specialists. As stated, we presume that this reflects a deliberate policy choice.

One of the Contributing Practitioners provided the following example from his practice where the inability to secure channel management prevented a certain channel from getting particular products. The case concerned a producer of beverages who wished to introduce its products in a restaurant chain, but did not want to risk that the restaurant chain would endanger the activities addressed to the classic retail channels by its other distributors across the EEA. Under the current VBER, it was however not possible to set up a distribution system, whereby both channels are managed separately without the risk that one channel interferes with the other. This example underscores that more possibilities to implement genuine channel management may lead to increased offerings on the market.

Another practitioner confirmed to have relied on the *Villeroy & Boch* case law of the Commission[50] to implement some form of channel management that escaped the prohibition of Article 101(1) TFEU. In many cases, this will not necessarily resolve the issue. *Villeroy & Boch* relied on the fact that the product ranges were different and that each channel was in need of its own product range. In such a case (and this is common practice) it will be possible to rely on the contractual product definition to separate the distribution channels. However, where the products are identical, but the customer profiles are different and require specialized attention, *Villeroy & Boch* would not immediately seem helpful and, more generally, the VBER regime does not offer real possibilities.

The potential impact for businesses and customers of relaxing the current regime in respect of customer-oriented channel management is further addressed in paragraphs 0-0 below.

VII. Option I – impact of implementing no policy change

The first Policy Option identified in respect of active sales restrictions in the Inception Impact Assessment is not to implement any policy change. In order to appreciate the potential impact of this Policy Option, it is helpful to summarize the key features of the current regime. The impact of this Policy Option correlates with these features. We then need to take on board the difficulties encountered with the current regime and to draw broader policy conclusions from maintaining the *status quo*. Even if the current policy is maintained, there are certain obvious possibilities to implement technical improvements that will facilitate the use of the future regime.

In bullet point format the key features of the current regime with regard to active sales restrictions aimed at territories and/or customer groups are the following:

- As a general rule, territorial active sales restrictions are hardcore for all distribution formats (selective distribution and non-exclusive distribution) except for cases where exclusive distribution is applied.
- The hardcore characterization is limited to distribution agreements of which the contract territories are situated within the EEA. Distribution agreements having their contract territories outside the EEA are not covered by Article 4(b) of Regulation 330/2010.

[50] *Villeroy & Boch* [1985] OJ L376/15, paragraph 37.

- With regard to exclusive distribution, active sales restrictions are excluded from the hardcore list if they (i) target a territory that is reserved for the supplier or that is exclusively allocated to a single distributor, (ii) in respect of the latter case, are imposed in all of the distribution agreements entered into by the supplier (including all of its connected entities) across the EEA and (iii) are not affecting the freedom to sell of the customers of the buyer.
- If these cumulative conditions are met, it does not matter in which type of distribution agreement the territorial active sales restrictions are included. This implies that also selective distribution agreements may contain an active sales restriction provided that the protected territory is not part of the selective network and meets the required standard of exclusivity.
- Location clauses are compatible with the hardcore list irrespective of the chosen distribution formula.
- Absolute end customer restrictions (covering both active and passive selling) can be imposed on wholesalers. This possibility applies irrespective of the chosen distribution formula.
- In a selective system, an essential distinction is that between authorized distributors, non-authorized resellers and end customers. An absolute ban can (and must) be imposed towards non-authorized resellers. Sales to any other type of customer (authorized distributors or end customers) cannot be restricted.
- In a non-selective system, customer restrictions (taking the form of an active sales restriction) can only be applied towards reserved and exclusive customer groups. The conditions that must be met are the same as those that apply to active sales restrictions aimed at exclusive territories.

Chapter V has explained that these features have triggered certain difficulties. While additional aspects will be addressed when discussing Policy Option II, it seems helpful to identify the following high-level consequences of maintaining the current regime.

There are in our opinion two features included in the current VBER regime pertaining to active sales restrictions that have a major impact on its practical relevance and usefulness:

- The parallel imposition requirement presents major (and in real business practice almost always insurmountable) difficulties for the introduction of active sales restrictions. It implies that every single distributor has a veto right (by not accepting the restriction in its agreement) over the introduction of active sales restrictions in the distribution agreements of the supplier (see, paragraph 0 above). This applies even in cases where the distributors are located in areas that are far removed from each other so that the practical effect of the inclusion of the active sales restriction in the relevant distribution agreement is nihil or close to nihil. The parallel imposition requirement represents presumably the single most important reason for practitioners to be very cautious when advising businesses to introduce active sales restrictions. The risk for mistakes is simply too great. Most experienced practitioners in this field of competition law will perceive this first feature as a decisive reason underpinning their recommendation not to proceed with active sales restrictions;
- The second is undoubtedly the prohibition to roll over the active sales restriction. In the vast majority of real live cases the EEA distribution system is not homogeneous and contains a mix of integrated importers/wholesalers, independent importers/wholesalers, integrated distributors, independent

distributors, independent sub-dealers and possibly even agents (see, paragraph 0 above). The inability to roll over the active sales restriction leads to incoherent results. Furthermore, the inability to roll over serves as an open invitation to circumvent the active sales restriction. A striking example from business practice is the need and related year-end stress to reach the contractually agreed annual volumes (either contractually agreed minimum volumes or volumes required to reach a certain bonus level). Towards the year-end, it is not uncommon that volumes are dumped in adjacent markets with the assistance of traders that purchase the products at very sharp prices. Such circumvention scenarios cannot be controlled in compliance with the VBER and, in effect, undermine the business logic of the imposition of active sales restrictions. Experienced practitioners will typically warn the business for the risk that the active sales restriction applies only at one level (*i.e.*, the level of the distributor with which the supplier has a direct contractual relationship) and rely on this factor to discourage the use of active sales restrictions as a reliable technique to contain the free-riding risk and to protect investments made by exclusive distributors.

As long as both the parallel imposition requirement and the prohibition to roll over are maintained (*status quo*), policy makers should realize that experienced practitioners (with a detailed understanding of the requirements relating to active sales restrictions under the VBER and the Vertical Guidelines) will discourage businesses from relying on active sales restrictions. The imposition of active sales restrictions creates legal uncertainty and does not offer the protection that businesses expect from this type of restrictions. Such practitioners will steer the business towards territorial exclusivity (coupled with a system of location clauses) or, when more sizeable investments and efforts are involved, even more so to selectivity. Considering our own practice of the past years, we do not recall a single instance where we have advised to introduce active sales restrictions in order to address free-riding concerns or to trigger and protect investments by the distributors. The input provided by the Contributing Practitioners points in the same direction (see, paragraphs 0-0 above).

Furthermore, these requirements present a trap for the unwary. Many practitioners and businesses that continue to work with active sales restrictions are in our experience often not familiar with the parallel imposition requirement and do not appreciate the consequences of the rolling over prohibition. They are not aware of the legal consequences of their failure to meet these requirements both in terms of the enforceability of the restrictions and the applicability of the block exemption to their distribution agreements.

Maintaining these two requirements will thus in our experience result in the following:

- Practitioners familiar with the details of the regime will continue to discourage the use of active sales restrictions.
- Practitioners less familiar with the regime may continue to rely on active sales restrictions but in the vast majority of cases in a manner that is not consistent with the requirements of the VBER (so that the active sales restrictions are hardcore and do not fall within the exception of Article 4(b)(i) of Regulation 330/2010).
- Both these consequences are not only suboptimal from the perspective of suppliers and distributors, but also for consumers. Given the link between the protection of investments (which may be deemed to serve the interests of consumers) and active sales restrictions, the decision not to use active sales restrictions or to use active sales restrictions in a setting where they are not enforceable does not necessarily match with the interests of consumers. It may either reduce the interest on the part of distributors to invest or steer

suppliers and distributors towards solutions that are less tailored to the needs and that may even be more restrictive than necessary (see, the unnecessary switch to selective distribution discussed in paragraph 0 above).

While not to be characterized as showstoppers, the *status quo* has also other tangible implications for the businesses that rely on the VBER which can usefully be considered when deciding on the future regime:

- The use of active sales restrictions under the block exemption regime remains confined to single exclusive distributors. Shared exclusivity is not eligible for active sales protection. As discussed, this can be addressed by means of formalistic solutions that are implemented for the sole purpose of complying with the single exclusivity requirement (see, paragraph 0-0 above). Conversely, in cases where it makes eminent economic sense to operate active sales restrictions, such protection cannot be offered where one or more distributors are not prepared to have their territories carved up. The carving up of territories into single exclusive contract territories may result in a more restrictive set-up than is needed in order to address the legitimate investment concerns of the relevant distributors (most certainly due to the parallel imposition requirement). A major consequence is that the single exclusivity requirement eliminates active competition between distributors that are prepared to accept a shared exclusivity regime. The increased competition that results from such a shared exclusivity regime would seem to benefit also consumers.
- The current regime renders it very difficult (and sometimes even impossible) to switch from one distribution regime to another. This observation applies, for instance, to switches from non-exclusive/non-selective distribution to exclusive distribution combined with active sales restrictions. In this case, the parallel imposition requirement will often be perceived as an insurmountable hurdle. Also, the need to carve up territories into single exclusive territories may cause transition difficulties. The same concern applies also to switches from non-selectivity to selectivity. A gradual switch (e.g., country-by-country) will be risky as it will not be possible to prevent distributors situated in the non-selective countries to sell to unauthorized traders in the selective countries. We describe this somewhat symbolically to our clients as the permanent time bomb endangering the switch. Hence, the current regime is drafted for distribution systems that are set up from scratch or that evolve gradually within the broader parameters of a given distribution formula. It does not facilitate more fundamental switches, even in cases where this makes eminent business sense and may match better with consumer expectations or needs.
- Genuine channel management is not possible under the current regime (see, paragraphs 0-0 above). It may prove difficult (particularly for smaller suppliers) to attract distributors which are highly specialized in a particular customer segment of the market without the assurance that their efforts will not be eroded by sales emanating (directly or indirectly) from the other distribution channels of the supplier. Genuine channel management requires most likely that these other distributors refrain from active and passive selling to the relevant customer segment and do not circumvent such a restriction via their downstream channels. A mere restriction of active sales at one level of the distribution chain will not be considered to offer any protection of significance against free riding on the efforts of the specialist. As stated, this may discourage channel specialists to accept products or services of certain (particularly) smaller suppliers. We assume that access to

specialist distributors, particularly for smaller suppliers, may work to the benefit of end customers.

- A further general policy choice concerns the ability to implement hybrid scenarios and notably those where different distribution formulas are applied across the EEA or where different formulas apply to different levels of trade. Such scenarios present difficulties under the current regime. The most outspoken consequence based on our experience is that related to the geographic differences. The inability to protect selective distribution against sales activities towards unauthorized resellers by network members located in non-selective markets may result in a broader roll-out of selective distribution across the EEA than strictly needed by the business.
- As to another hybrid hypothesis, several practitioners refer to the need or usefulness to apply different distribution formulas at different levels of trade. This makes in practice only a difference under the current regime and thus triggers difficulties, if the relevant mix includes selective and non-selective distribution. We have not seen in our practice that this issue is high on the list of the businesses that wish to switch to selective distribution. This may in part be a consequence of the fact that, based on the current VBER regime, practitioners (including ourselves) make it clear from the outset that such a scenario triggers hardcore issues. The usefulness of such a hybrid set-up will obviously depend on the sector and, in particular, the efforts required at the importer/wholesale level with regard to its allotted territory.

Without pre-empting on a discussion of the Policy Options, there are certain areas where the current regime of the VBER (if it is maintained) can be improved and made more user-friendly. These are purely technical improvements and apply in a "no policy change" context. It would indeed be helpful if the future Guidelines provide additional clarification on the following:

- the scenarios that are covered by the concept of 'territory reserved to the supplier';
- the freedom of the parties to define the reserved and exclusively allocated territories;
- the concept of 'customer group';
- the limitation of the scope of application of Article 4(b) of Regulation 330/2010 to intra-EEA scenarios;
- the ability to roll-over an active sales restriction by having three- or multi-party agreements;
- the explicit introduction of the parallel imposition requirement in the text of Article 4(b)(i) of Regulation 330/2010;[51]
- the absence of the need to impose an active sales restriction on the supplier in order to meet the parallel imposition requirement;
- the absence of the need to comply with the parallel imposition requirement towards territories reserved to the supplier;

[51] In the event that the parallel imposition requirement is kept, it is highly advisable for reasons of legal certainty to introduce this requirement within Article 4(b) of Regulation 330/2010 and not to mention it merely in the Vertical Guidelines. If it is decided not to include it explicitly in Article 4, a more explicit treatment of the requirement in the Vertical Guidelines seems to be absolutely necessary so as to create greater awareness.

- a more explicit statement that it is possible both in a non-selective and a selective environment (quantitative selectivity) to work with exclusive appointments (no appointment of additional distributors within a given territory);[52]
- a more explicit confirmation that active sales restrictions can be imposed in selective distribution agreements if aimed to protect an exclusively allocated territory in an exclusive distribution scenario (so that the parallel imposition requirement can be met throughout the EEA).[53]

It is obvious that, depending on the policy choices made for the future regime, certain of these observations may become redundant.

More generally, the guidance offered in the future Vertical Guidelines should be more elaborate and tested with the common users of the legal instrument so as to avoid traps for the unwary and unnecessary disputes. The lack of understanding of the active sales regime (as it is currently formulated) should not be underestimated. As the legal consequences are severe (qualification as hardcore; inapplicability of the block exemption to the distribution agreement as a whole; negative presumption regarding the availability of an individual exemption), it is essential that a high degree of clarity is created on the applicable regime and its requirements.

VIII. Option II – impact of relaxing current framework to offer suppliers more flexibility when designing their distribution system

Policy Option II implies that the current framework is relaxed to offer suppliers more flexibility when designing their distribution systems in line with Article 101 TFEU. We propose to distinguish between two key changes and additional Policy Options which may contribute to more flexibility and a more effective implementation of active sales restrictions.

A. Key changes

As mentioned, practitioners aware of the details of the current active sales restriction regime will cautiously steer the business away from this possibility to protect exclusive distributors. Hence, if the policy makers believe that this type of restriction should be preserved as a tool to address free-riding concerns and, more generally, to encourage and protect investments made by exclusive distributors, it is recommended to remove the obstacles that discourage the application of the current regime. It is our assumption that, to the extent that active sales restrictions may contribute to such positive effects, they are consistent with the consumer welfare objectives underpinning the application of the competition rules.

1. Parallel imposition requirement

A first important change is the removal of the parallel imposition requirement from the future regime. The practical difficulties with this requirement were already partially addressed when the switch was made from Regulation 2790/99 to Regulation 330/2010, by no longer imposing the requirement on the supplier in relation to

[52] The introductory sentence of paragraph 57 of the Vertical Guidelines is often misread in this respect.

[53] It is unclear whether this possibility extends to reserved territories. Paragraph 56 (with its cross-reference to paragraph 51) of the Vertical Guidelines is not necessarily clear in this respect.

territories exclusively allocated to single distributors. This change was helpful but insufficient to restore confidence in the active sales regime. The requirement as it currently stands, while theoretically understandable, is disproportionate and, in fact, unworkable in practice. Absent truly exceptional scenarios, practitioners will simply not take the risk of advising the use of active sales restrictions as long as the parallel imposition requirement remains in place. The Contributing Practitioners have voiced this position very clearly. This position is also consistent with our own current practice.

The removal of the parallel imposition requirement would imply that suppliers and distributors may include active sales restrictions in such cases where this is realistic and relevant and thus not necessarily in every single distribution agreement concluded by the supplier (including all of its connected undertakings):

- Without the parallel imposition requirement, a supplier can offer protection against active sales from those distributors, with whom the supplier is (practically and realistically) able to negotiate such a restriction. We have provided earlier in this Report examples of a number of scenarios where it is simply not workable to cause the supplier (and its connected undertakings) to inject active sales restrictions in all of their distribution agreements (see, paragraphs 0-0 above). In our experience and that of the Contributing Practitioners, the parallel imposition requirement is in practice not realistic and, if properly understood, a showstopper for the application of active sales restrictions in the vast majority of distribution set-ups.
- The removal of the parallel imposition requirement would also enable suppliers and distributors to limit the use of active sales restrictions to such cases where the protection is truly relevant. If a distributor is exclusively appointed in a Belgian city on account of particular efforts and investments made to the benefit of the supplier and the local customers, it would not seem particularly relevant that the Maltese distributor is subject to an active sales restriction towards that particular Belgian city. The relevant protection concerns most likely the distributors in the adjacent territories and not necessarily in distant parts of the EEA. The fact that active sales restrictions are included in such distant distribution agreements lacks relevance, which in turn makes it more difficult to explain why the failure to do so amounts to a hardcore issue.

The Belgian/Maltese example underscores that the failure to meet the parallel imposition requirement has legal consequences that are disproportionately severe. It is impossible to explain to businesses that each distributor (even those most far removed from the exclusive territory concerned) holds a veto right over the ability to operate active sales restrictions in other parts of the EEA. This hardcore qualification combined with the legal uncertainty that the entire network cannot be covered steers practitioners away from the use of active sales restrictions, even in cases where this would present a useful tool to serve the interests of suppliers, distributors and customers.

The question has been raised in which cases, if there would no longer be a parallel imposition requirement, the active sales restrictions can or should be included. In a block exemption environment (which relies on a 30% market share limit) we suggest that this decision should be left to the market. It seems impossible to regulate or define in general terms the cases where the use of active sales restrictions is realistic and relevant.

2. Rolling over prohibition

A second key change that will influence the future use of active sales restrictions concerns the rolling over prohibition. The rolling over prohibition leads to incoherent

market situations from the moment that a distribution network is not structured in a homogeneous manner across the EEA. This will be so in the vast majority of cases and apply in particular to less powerful and resourceful suppliers. Such suppliers will typically work with a mixture of wholly-owned and independent distribution channels (particularly at the importer/wholesale levels).

If the policy makers wish to preserve the use of active sales restrictions as a tool available to businesses under the future regime, a partial relaxation of the rolling over prohibition is required. We believe that the rolling over prohibition should in that case not apply to any member of the structured distribution network of a given supplier, irrespective of the level where the network member is active (importer – wholesale – retail (including sub-distribution)). A structured distribution network includes independent distributors that have entered into a written distribution agreement that formalizes the distribution relationship with either the supplier or a party that has, directly or indirectly, been given distribution rights by the supplier, irrespective of the level of trade at which the relevant parties are active. Such a formalized distribution relationship will typically grant the distributor a right to be supplied with the relevant products (*i.e.*, the so-called contract products), authorize the distributor to use certain product or marketing materials or trademarks, or to receive certain support when performing its distribution function.

The elimination of the rolling over prohibition in the context of the structured distribution network of a given supplier avoids scenarios such as those described in paragraph 0 of this Report. This solution therefore addresses the difficulties caused by the lack of homogeneity of the networks across the EEA. Such difficulties seem to lead to a rather arbitrary application of active sales restrictions depending on the structure and composition of the distribution network of a given supplier. As stated above, the assumption that such networks are homogenous does not match with our practical experience and that of the Contributing Practitioners.

3. Conclusion

Based on our practical experience and that of the Contributing Practitioners the elimination of the parallel imposition requirement and the limitation of the rolling over prohibition are essential to place active sales restrictions (as a tool to protect investments) back on the menu of realistic options to be considered by practitioners. Such modifications would seem to benefit suppliers, distributors and consumers alike as a lawful, realistic and relevant application of the concept may be assumed to match their respective interests.

B. Other possibilities

We identified four other areas to adapt the regime of active sales restrictions under the current VBER that would give suppliers more flexibility to design their distribution systems according to their needs and in line with Article 101 TFEU. Such additional flexibility operates not to the sole benefit of the suppliers, but may be deemed to serve also the interests of distributors and consumers. While there may conceivably be other areas that can be considered, these are the areas that most prominently result from the input of the Contributing Practitioners, as well as from our own practice.

1. Rolling over prohibition – facilitating circumvention

In addition to the key changes proposed in paragraphs 0-0 above, the treatment of the rolling over prohibition could be further adapted so as to increase the likelihood that active sales restrictions address freeriding concerns and incite investments by the network. This is for us not a key change, but a policy choice.

A first possible change is to address circumvention scenarios whereby low margin sales to traders are used to sell into other territories. This represents a genuine risk for which practitioners will have to warn the business (see, paragraph 0 above).

It would be helpful if the future Vertical Guidelines refer to the ability to rely on a breach of the active sales restrictions in cases where a distributor deliberately circumvents the restriction by involving an independent reseller. Such circumvention involves an intentional element and it would be for the party relying on the active sales restriction to carry the burden of proof in this respect. It is reasonable to assume that this is no more than an application of the principle of good faith performance of the active sales restriction. However, as the law stands and given the hardcore risk, it may be perceived as helpful if it is clarified that any such deliberate circumvention can be addressed by the supplier without running the risk of a hardcore infringement. In the case of a conflict, it will ultimately be the court that will decide whether the requirements of a deliberate circumvention scenario are met.

A second possible change takes the same logic one step further and eliminates the roll over prohibition completely. This implies that within a given chain of distribution or resale agreements it is possible to roll-over the active sales restriction without limitation. The argument in support of such a change would be that passive sales are obviously left free and that internet sales (generally being considered as passive sales by practitioners and businesses (see, paragraphs 0 and 0 above)) are much more prominent now and would remain unaffected by the change.

Needless to say, both changes will render the use of active sales restrictions more attractive. As stated, we believe that only the elimination of the rolling over prohibition within structured distribution networks is a key change and that these additional changes merely serve to increase the attractiveness of active sales restrictions as a tool to address freeriding or to incite investments. The difference between the two is that the key change addresses, in our view, a lack of coherence in the current regime leading to arbitrary results from the moment that distribution networks are not structured perfectly homogenously. The additional change concerns the position of independent resellers (such as traders) that are not part of the formalized distribution network and simply engage in resale activities. The rolling over prohibition does not necessarily trigger the same arbitrary consequences if it applies in the relationship between a member of the structured distribution network and an independent reseller that is not part of such network. Such application boils down to a scenario where, as soon as a product leaves the structured distribution network, an independent reseller is free to sell to whom it wants and where it wants within the EEA. It is a policy choice (and not a remedy to a conceptual problem) whether this additional step is taken and the rolling over prohibition is also removed in the case of sales to such independent resellers. If the policy makers do believe that active sales restrictions may trigger positive effects and wish to promote its use (rather than certain alternatives) this additional step may prove however extremely useful to put this type of restrictions back on the list of realistic options to consider when protecting investments by the distribution network.

2. Shared exclusivity

The inapplicability of the VBER to shared exclusivity would seem to exclude inadvertently a number of scenarios, which may in fact be more pro-competitive than single exclusivity scenarios (see, paragraphs 0-0 above).

Shared exclusivity is understood as a set-up in which multiple distributors are appointed in a specific territory/towards a customer group. The distributors are named and benefit from a contractual guarantee that no additional distributors will be appointed. If such contractual framework applies, it would, in our view, not seem necessary to fix the maximum number of shared distributors that is allowed to benefit

from an exemption under the VBER/Vertical Guidelines. There would not be a risk that additional distributors can be added as the suppliers see fit, since this would always require the consent of the other appointed distributors in the shared exclusive territory. On account of this balance of interests, it is reasonable to assume that situations of shared exclusivity will be rather stable and, if additions are made, they will respond to a genuine need accepted by the supplier and each of the distributors.

In our experience, the extension of the active sales regime to situations of shared exclusivity may indeed contribute to a more flexible regime that allows suppliers and distributors to better adapt the distribution system to their business needs, without necessarily increasing restrictive effects. Shared exclusivity would be particularly useful to facilitate network transitions. Also, we have come across business cases where the supplier wishes to protect the existing distributors and their investments, but there is no business reason to divide a territory into single exclusive territories between existing distributors. Any such division would be the result of formalistic compliance with the VBER. A change towards shared exclusivity would therefore also do away with the artificial creation of exclusive territories for the sole reason of complying with the conditions of Article 4(b)(i) of Regulation 330/2010.

Based on our experience, we do not see any immediate risk with a switch from single exclusivity to shared exclusivity. The distributor has no incentive to accept shared exclusivity if this would not provide it with a sufficiently large territory to set up a profitable business and the supplier has no incentive to offer shared exclusivity if it would undermine the incentives for the distributors to invest in its products. Furthermore, if shared exclusivity requires a contractual commitment of the supplier not to appoint additional distributors within the territory without the consent of all of the incumbent distributors, the creation of shared exclusivity may be assumed to be based on a negotiation equilibrium involving all parties concerned. This would seem a fair assumption under the VBER given that the market share limit of 30% may be expected to exclude scenarios where a supplier or distributor has market power to such an extent that it could result in abuses.

Shared exclusivity would moreover also not increase the risk of market partitioning. In fact, the opposite would be the case as competition between the distributors included in the same territory (both in terms of active and passive selling) remains free. In that sense, a system of shared exclusivity tends to increase intra-brand competition that otherwise, on account of the use of single exclusive distributors in combination with the parallel imposition requirement, would be more restricted. As consumers would benefit from such increased intra-brand competition, this change would also operate to their advantage.

3. Customer-oriented channel management

Another area where a relaxation of the rules may contribute to more flexibility in the interest of both suppliers and distributors concerns customer-oriented channel management.

In the event that the policy makers would accept the key change relating to the rolling over prohibition, the difficulties in respect of customer-oriented channel management may already be addressed to a considerable extent. This would ensure that all distributors that are appointed as part of the structured distribution network will be held to respect an active sales restriction targeted at specified customer groups.

In addition, elimination of the parallel imposition requirement will also facilitate customer-oriented channel management by the supplier. There is only a real business need to prohibit distributors from selling actively to a specific customer group, when they are in a position to free ride upon the sales efforts and investments of an exclusively appointed distributor (the channel specialist). The fact that an active sales

restriction under the current regime constitutes a hardcore restriction, merely because one or more of the distributors has failed to accept an active sales restriction towards a particular customer group, seems not to justify the limitation of possibilities to create a meaningful system of customer-oriented channel management.

Hence, the concerns expressed with regard to the inability to set up channel management are addressed to a large extent by the application of the recommended key changes. Any further step to facilitate channel management would most likely affect the ability to engage in passive sales (see, e.g., Article 4(2)(b)(i) of Regulation 316/2014). We assume that such a step would only be considered if, based on experience, the protection of customer-oriented channels is perceived to incite more investments by the channel specialists and that such investments and the related benefits for consumers outweigh the possible restriction of competition resulting from the limitation of passive sales. Another positive effect of such channel management that may be taken into consideration is the potential willingness of the channel specialists to accept the representation of smaller suppliers and not just the leading players. We have not conducted any systematic research in this respect and the examples presented by the Contributing Practitioners and those resulting from our own practice are insufficient to cast an opinion in either direction.

4. Combination of exclusivity/selectivity at different trade levels

The hybrid situation of exclusivity and selectivity at different trade levels is currently addressed in paragraph 63 of the Vertical Guidelines. As described above (see, paragraphs 0-0 above), the main difficulty in such a hybrid situation stems from the uncertainty when applying the conditions of paragraph 63 of the Vertical Guidelines and the fact that it continues to trigger a hardcore restriction.

If the policy makers wish to facilitate the possibility for suppliers to set up a hybrid scenario covering different trade levels (essentially exclusivity upstream and selectivity downstream), the approach adopted in paragraph 63 of the Vertical Guidelines must be abandoned at least in the following respects:

First, it is not helpful to make the exemption dependent on whether or not it is "*practical to specify in a contract the required promotional activities*" as provided in paragraph 63 or on similar tests that are open to wide interpretations. Such conditions cause legal uncertainty and will trigger disputes by market participants who have an interest in challenging the distribution set-up.

Second, in light of the negative presumption that applies to hardcore restrictions, there is only one technical solution that offers businesses sufficient legal certainty, namely to provide for an additional exception covering active sales restrictions under the revised VBER. Such exception should allow for active sales restrictions at the wholesale level, in order to protect the investments by wholesalers in their respective selective retail networks.

We believe that such a change is less fundamental than the recommended key changes, but could be considered a tool to promote investments in the deployment and maintenance of selective distribution systems at the retail level in a given market. As stated, if it is the intention to offer such a possibility, the two aforesaid observations (see, paragraphs 0-0) should be duly taken into consideration.

Somewhat similarly to the issue of channel management, our own practice and the examples offered by the Contributing Practitioners do not provide a strong indication as to the direction to be taken in this respect. This may largely be a consequence of the fact that the envisaged set-up (including the possibility to impose active sales restrictions at the wholesale level) results in a hardcore issue (incompatibility with Article 4(d) of Regulation 330/2010) and that such issue causes practitioners to discourage businesses from adopting such direction. In that respect, it is somewhat

surprising that the Commission Staff Working Document on the Evaluation of the VBER refers to a confirmation that combining exclusivity at the wholesale level and selectivity at the retail level would be "common practice". This observation would not necessarily apply to our practice or that of the Contributing Practitioners and suggests that already now set-ups are commonly applied that are not compatible with Article 4(d) of Regulation 330/2010.

IX. Option III - impact of exempting sales restrictions from outside the territory in which the selective distribution system is operated

The third Policy Option in respect of active sales restrictions proposed in the Inception Impact Assessment provides "ensuring more effective protection of selective distribution systems by allowing restrictions on sales from outside the territory in which the selective distribution system is operated to unauthorized distributors inside that territory".

This Policy Option therefore implies a combination of a territorial and a customer restriction for non-selective distributors, as it restricts selling inside the selective territory (territorial restriction) to non-authorized distributors (customer restriction). As described above (see, paragraphs 0-0 above), such sales restrictions currently do not benefit from an exemption under the VBER. The exception of Article 4(b)(iii) of Regulation 330/2010 provides for a restriction not to sell to unauthorized distributors by members of the selective system itself. If the policy makers were to consider Policy Option III, the current rules would need to be adapted by allowing the extension of the restriction to all buyers of the supplier.

As already set out above (see, paragraphs 0-0 above), the fact that non-selective distributors are currently not prevented from selling to unauthorized distributors within a selective territory is a cause of major concern for many businesses when the selective distribution system does not cover the entire EEA. In such case, there is always a risk that the selective system is undermined by sales from outside the selective territory to unauthorized distributors in the selective territory. Under the current VBER regime, the only option to avoid such a business risk is by implementing selective distribution across the entire EEA. This option may not necessarily meet with the business needs and may restrict competition more than is necessary (by reducing intra-brand competition in the markets that would otherwise remain non-selective).

We have come across multiple business cases in which businesses encountered difficulties as a result of the fact that sales from outside the selective territory to unauthorized distributors within that area cannot be prevented. The two examples discussed above (see, paragraphs 0-0 above) illustrate the issue. We believe that suboptimal solutions have been applied solely on account of the fact that a supplier wished to avoid that its selective distribution system risked to be undermined. It is indeed difficult to convince the members of a selective distribution network to stick to the selectivity requirement (prohibition of sales to unauthorized distributors) when confronted with sales to unauthorized distributors originating abroad, and more particularly from non-selective countries where the same investments are in most cases not made.

For reasons of overall coherence of the block exemption regime applicable to selective distribution systems and in order to accommodate hybrid scenarios that are more consistent with the actual business needs, we believe that it makes eminent sense to extend the exception of Article 4(b)(iii) of Regulation 330/2010 to cover also non-authorized distributors located outside the selective territory.

In order to make the implementation of this Policy Option effective, the ability to prevent sales to unauthorized distributors should not be confined to the first tier of the supplier's non-selective distribution network. Such a limitation would not solve the issue and is furthermore inconsistent with the coherent application of selective distribution systems. Similarly to the distributors within the selective territories, the selectivity requirement should apply at all levels of the distribution chain (including resellers or traders that do not belong to the structured distribution network of the supplier). The failure to extend the exception to such additional levels would be an open invitation to mount circumvention scenarios by involving third parties to conduct the relevant sales. If that were possible, the adaptation included in the new regime would serve only a very limited purpose and risks not to address the real issue. If the intention is to safeguard the coherence of the system of selective distribution, the selectivity requirement should apply within the non-selective countries in exactly the same manner as it does in the selective countries.

X. Overall conclusions and recommendations

When deciding on the way forward based on the stated Policy Options, the following observations stemming from the practice of the Contributing Practitioners and our own practice may serve as a useful background:

- While it may be assumed that active sales restrictions may present a useful tool to address free-riding concerns and to promote investments by the distribution network, they are no longer favoured and recommended by practitioners who are familiar with the relevant requirements stated in the VBER and the Vertical Guidelines. There is a clear trend towards recommending the use of selective distribution, even in cases where active sales restrictions linked to an exclusive distribution set-up may also potentially achieve the desired objectives.
- The relevant requirements are complex and there is a genuine risk that the lack of awareness of the details of these requirements is underestimated. This risk is enhanced by the fact that Article 4(b) of Regulation 330/2010 is densely formulated and that the Vertical Guidelines are cryptic in their description of the requirements.
- The two most important aspects that explain the lack of attractiveness of active sales restrictions to practitioners are the parallel imposition requirement and the rolling over prohibition. The problems presented by these two aspects (and particularly the parallel imposition requirement) are essentially of a technical nature and result from a need to ensure compliance with the VBER. In other words, they do not necessarily stem from any particular business or other non-legal preference.
- The business reality is seldom that a homogenous distribution system has been rolled out or that suppliers can start from scratch when deciding on, and implementing or modifying their distribution networks. In this context it is important to underscore that relevant circumstances (which may include the market position of the supplier, the local positioning of the supplier's products and brands, the available distribution channels and the like) may call for a differentiated distribution approach, which may include the combination of selective and non-selective distribution systems in different geographic areas.
- Even though it is not excluded that online sales may qualify as active sales, practitioners tend to treat them in their advisory practice systematically as passive sales. In addition, it is difficult to deny that the relative importance of online sales compared with offline sales has increased in recent years. It is reasonable to assume that the COVID-19 crisis has enhanced this trend. As a result, in many sectors the proportion of the business that can be rendered subject to an active sales restriction has gone down compared with the position at the time of the adoption of Regulations 2790/99 and 330/2010. Hence, at the present time the potentially negative impact of active sales restrictions on intra-brand competition (and also on inter-brand competition) may be deemed less when compared with the position during the period of application of the previous and the present block exemption regulations.
- In practice there is a considerable difference between the application of a block exemption regime and the switch to a self-assessment. A self-assessment aiming to address difficulties with the requirements related to active sales restrictions will be perceived in almost all instances as a "no go". The failure to meet one or more of these requirements triggers a hardcore problem and the related negative presumption of the incompatibility of the

agreement (and not just the active sales restriction) with Article 101(3) TFEU. This is a risk that practitioners will not want to take. The consequence of all this is that the block exemption regime will in practice serve as the relevant regime both for networks falling within its scope of application and networks that fail to meet the conditions for the application of Regulation 330/2010 (such as the market share limit). Hence, in practice there is in most instances not a realistic self-assessment alternative for active sales restrictions that do not adhere to the requirements of Article 4(b)(i) of Regulation 330/2010.

We recommend not to adopt Policy Option I. Policy Option I would in our experience mean that the possibility to use active sales restrictions as an exception to the hardcore restrictions of Article 4(b) of Regulation 330/2010 remains in most cases only theoretically available. In practice and depending on the awareness and knowledge of the conditions linked to Article 4(b)(i) of Regulation 330/2010, businesses and practitioners will either (continue to) steer away from this exception or they will tend to apply it incorrectly (e.g., because they fail to implement the parallel imposition requirement correctly). If the Commission intends to enable businesses to make genuine use of active sales restrictions in the future and believes that active sales restrictions may present a useful tool to trigger positive effects that are also beneficial to consumers, the *status quo* does in our view not really present an option.

With regard to Policy Option II, we recommend strongly to eliminate the requirements included in the current regime that discourage the use of active sales restrictions on technical/legal grounds. The first such requirement is the parallel imposition requirement. The problem with this requirement is that it is very difficult and often impossible to meet in practice. The elimination of this requirement would in our view not have a negative impact on the effectiveness and the positive effects of active sales restrictions within an exclusive system. The second requirement is the rolling over prohibition. In order to render the active sales regime workable (particularly for distribution systems that are not structured homogeneously) it would be appropriate if the various members of a structured distribution system of a given producer or supplier can all be rendered subject to an active sales restriction. As stated in the Report, the protection offered by active sales restrictions in cases where the level of vertical integration may differ across the EEA or the distribution set-up is not identical in all countries of the EEA becomes otherwise incoherent and even somewhat arbitrary. Without these proposed changes we believe that businesses and practitioners will not perceive the use of active sales restrictions as a realistic and relevant tool, while the stated (technical) requirements would also not be needed to protect consumer welfare.

While less critical than the aforesaid proposed changes, a switch from single exclusivity to shared exclusivity, whereby the number or identity of the shared exclusive distributors is contractually agreed, would in our view make eminent sense. We do not see why such a switch would increase possible negative effects (particularly at a time when internet sales are very prevalent) and it would do away with the need to engage in formalistic compliance by splitting somewhat artificially territories into single exclusivities. This is all the more so where such an artificial split reduces intra-brand competition more than may be needed to achieve the desired positive effects.

Other possibilities for changes include the complete abolishment of the rolling over prohibition (and not just for the structured distribution network), increased protection for customer-oriented channel management and the freedom to use active sales restrictions at the wholesale level while operating a selective distribution system at the retail level. We believe that such changes may render the use of active sales restrictions more attractive, but we deem them less critical than the ones identified

above and lack experience based on real business examples to adopt a firmer position in respect of such possible changes.

Based on our practical experience we believe that Policy Option III is very valid. The ability to safeguard the integrity of a selective network across the EEA by ensuring that non-selective distributors can be contractually prevented from reselling to unauthorized traders active in selective territories makes eminent sense. Not only would such a change result in a more coherent and logical regime, it eliminates also the need to implement set-ups that go further than is needed to meet the business needs and to trigger the desired positive effects (e.g., by rolling out very light selective distribution networks in certain countries for the sole reason of avoiding gaps in the selective systems operated in other countries).

We furthermore believe that Policy Option II and Policy Option III can be applied in tandem without there being any additional negative impact resulting from combining both options. Both policy options address different concerns and allow to increase the efficiency and relevance of the VBER for businesses and consumers.

In summary, our recommendations are:

- Not to implement Policy Option I.
- To implement Policy Option II with, as a minimum, the complete elimination of the parallel imposition requirement and the limitation of the rolling over prohibition to resellers situated outside the structured distribution network of the supplier.
- To implement Policy Option II by extending the exception of Article 4(b)(i) of Regulation 330/2010 to situations of shared exclusivity.
- To assess further, as a part of Policy Option II and taking into account the increased levels of internet selling, whether it is advisable to abolish the rolling over prohibition completely, to increase the protection offered in cases of customer-oriented channel management and to allow active sales restrictions at the wholesale level in situations where selective distribution is applied at the retail level. Further assessment would seem appropriate as our practical experience and that of the Contributing Practitioners seems insufficient to draw any firm conclusions in this respect.
- To implement Policy Option III (in combination with the recommended changes under Policy Option II) so as to ensure that the coherence and integrity of selective distribution systems is safeguarded in cases where the supplier has not implemented selective distribution across the EEA.

Abstract

This report contains expert advice on "*the use of active sales restrictions in different distribution models and combinations of such models*". It is based upon the experience resulting from the practice of the authors and relies also on input from practitioners in various Member States.

The report describes the general regulatory framework and maps the difficulties encountered in respect of active sales restrictions under the VBER. The authors assess the impact of three different policy options identified as part of the Inception Impact Assessment. They formulate recommendations regarding each of the Policy Options, which are illustrated with business examples.

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