Working paper:

Distributors that also act as agents for certain products for the same supplier

Introduction

1. The European Commission is currently reviewing the Commission Notice providing Guidelines on Vertical Restraints ("Vertical Guidelines"), within the broader context of the review of Commission Regulation (EU) No 330/2010 ("Vertical Block Exemption Regulation", "VBER")[1]. The application of Article 101 TFEU on distribution agreements as well as agency agreements is dealt with in the Vertical Guidelines, to which this working paper relates. In the context of this review, stakeholders have indicated that guidance in the Vertical Guidelines is not sufficiently clear as to whether an undertaking active on a downstream market may act both as a genuine agent and as an independent distributor for different products of the same supplier (so-called "dual role" agents). In addition, DG Competition has noted a trend towards the increased use of models combining agency and distribution in consumer goods markets, under which a single undertaking combines the functions of agent and independent distributor for the same principal/supplier.

2. Against that background, the present working paper seeks to discuss how Article 101(1)[2] of the Treaty on the Functioning of the European Union ("TFEU") may be applied to situations where a distributor of certain supplier also acts as agent on behalf of that same supplier (the "principal"). This working paper has been prepared in the context of the ongoing review of the VBER and the Vertical Guidelines and is without prejudice to any changes that could arise from that review. Additional experience gathered from monitoring market developments following the publication of this working paper will be taken into account in the review process and reflected in the revised Vertical Guidelines. This working paper therefore does not commit the Commission and only contains provisional views of DG Competition in preparation of the adoption of the revised Vertical Guidelines (expected in May 2022). In addition, this working paper is without prejudice to the case law of the Court of Justice of the European Union (the "Court") on the application of Article 101 TFEU to vertical agreements.

3. DG Competition had informal discussions with stakeholders envisaging the use of models within which the same undertaking acts both as agent and independent distributor for different products of the same supplier[3]. These instances concern suppliers of differentiated products that have so far distributed their products using independent distributors. These suppliers of differentiated products were considering distributing a limited number of models or types of specific products (typically of higher quality or presenting novel features) under an agency agreement, by entering into such agreements with their existing independent distributors already active on the relevant market. The price of the products sold under the

[1] Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices.

[2] This working paper only focuses on the applicability of Article 101(1) TFEU to agents acting in a dual role. It does therefore not concern the application of Article 101(3) TFEU to agreements that would fall within the scope of Article 101(1) TFEU.

[3] Commission's Staff Working Document, Evaluation of the Vertical Block Exemption Regulation, 8 September 2020, SWD(2020) 173 final, page 148.

agency agreement would thus be set by the supplier, whereas the distributors would continue to sell other products of the supplier as independent distributors, together with the products of competing suppliers. Therefore, to the extent that other scenarios have not yet been brought to DG Competition's knowledge, and without prejudice to the position that the Commission may ultimately take on those scenarios, this working paper only relates to markets comprising differentiated products that present distinct characteristics, such as higher quality, novel features or additional functions, which allow to distinguish objectively between those covered by the agency agreement and those distributed independently. Similarly, this working paper does not discuss situations where the company acting as agent and distributor is an online platform and is without prejudice to the question of whether the agency concept is applicable to online platforms.

Framework of assessment

Applicability of Article 101 TFEU

4. Paragraphs 12-21 of the Vertical Guidelines provide guidance on the application of Article 101 TFEU with regard to agency agreements. These paragraphs explain that all obligations imposed on the agent in relation to the contracts concluded and/or negotiated on behalf of the principal under an agency agreement fall outside the scope of Article 101(1) TFEU, as far as the selling or purchasing function of the agent forms part of the principal's activities and the principal bears the commercial and financial risks related to the selling or purchasing of the contract goods or services. However, as far as the agent remains a separate undertaking from the principal, provisions that concern the relationship between the agent and the principal fall within and may infringe Article 101(1) TFEU.

5. Paragraph 49 of the Vertical Guidelines provides that in the case of genuine agency agreements, the principal normally establishes the sales price, as the agent does not become the owner of the goods. By contrast, where such an agreement cannot be qualified as a genuine agency agreement for the purposes of applying Article 101(1) TFEU, restricting the agent from sharing his commission with the customer, without reducing the income for the principal, constitutes a hardcore restriction under Article 4(a) of the VBER[4].

[4] The Court of Justice has held on several occasions that agreements that impose upon retailers minimum or fixed retail prices, thereby restricting the ability of those retailers to determine their resale prices independently, restrict competition by object within the meaning of Article 101(1) TFEU. Moreover, agreements or concerted practices that directly or indirectly have as their object the restriction of the buyer's ability to determine its sale price are considered hardcore restrictions under Article 4(a) of the VBER. See Case 243/83, 3 July 1985, *Binon v AMP*, paragraph 43; Case C-311/8, 1 October 1987, *VVR v Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten*, paragraph 17; Case C-27/87, 19 April 1988, *SPRL Louis Erauw-Jacquery v La Hesbignonne SC*, paragraph 15.

Conditions for an agency agreement to fall outside the scope of Article 101 TFEU

6. An agency relationship will only fall outside the scope of Article 101(1) TFEU if the agent does not bear any of the risks associated with the contracts negotiated on behalf of the principal and operates as an auxiliary organ forming an integral part of the principal's undertaking[5].

7. However, where a genuine agent undertakes other activities for the same or other suppliers at its own risk, there is a risk that the conditions imposed on the agent for its agency activity will influence its incentives and limit its decision-making freedom when it sells products as an independent activity. These risks are particularly acute in instances where the products covered by the agency relationship and those distributed independently by the agent belong to the same product market. In particular, there is a risk that the pricing policy of the principal for the products sold under the agency agreement will influence the incentives of the agent/distributor to price independently the products that it sells as an independent distributor.

8. In addition, the use of such a system combining agency and independent distribution for the same supplier raises difficulties in distinguishing between investments and costs that relate to the agency function, including market-specific investments, and those only related to the independent activity pursuant to the cost allocation principles, as set out in paragraphs 12-22 below. The assessment of whether an agency relationship meets the conditions set out in paragraphs 12-21 of the Vertical Guidelines to be considered genuine and to fall outside the scope of Article 101 TFEU can therefore be particularly complex in those cases[6]. This is of particular concern if the agent undertakes other activities as an independent distributor for the same principal in the same product market. Conversely, these concerns are less likely to arise if the other activities undertaken as an independent distributor concern a different product market[7]. More generally, the less interchangeable the products are, the less likely are the risks described in this paragraph and in paragraph 7 to occur.

9. Against this backdrop and notably the difficulties associated with clearly distinguishing between investments and costs related to the agency agreement and those related to independent distribution in scenarios concerning the same product market, the agency model has, to DG Competition's knowledge, generally been operated so far on the basis of agency agreements covering the entirety of the principal's products in a particular product market. This is also reflected in paragraph 16(g) of the Vertical Guidelines, which sets out that an agreement will generally be considered a genuine agency agreement where the agent *"does not undertake other activities within the same product market required by the principal, unless these activities are fully reimbursed by the principal"*. This provision covers exceptional cases in which the principal requires the genuine agent to carry out other activities in the same product market, which are by definition of more limited nature compared to the main task of

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[5] See Case C-217/05, 14 December 2006, *Confederación Espanola de Empresarios de Estaciones de Servicio v CEPSA*, paragraph 43; Case 311/85, 1 October 1987, *ASBL Vereniging van Vlaamse Reisbureaus contre ASBL Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten,* para.20.

[6] See Joined cases 40 to 48, 50, 54 to 56, 111, 113 and 114/73, 16 December 1975, *Coöperatieve Vereniging "Suiker Unie" UA and others v Commission of the European Communities*, paragraphs 537-557.

[7] See Case T-325/01, *DaimlerChrysler AG v Commission*, paragraphs 100 and 113.

distributing the principal's products under the agency model (i.e. the agency agreement is considered as typically amounting to full or close to full agency in the same product market, possibly including minor independent activities).

10. To be able to assess whether an agency agreement falls outside the scope of Article 101(1) TFEU in instances where an agent has a dual role within the same product market, it is important to be able to effectively delineate the activities that are covered by the agency agreement and the risks associated to them. In scenarios, such as those presented to DG Competition, it may be possible to distinguish more easily between the risks and incentives associated with the distribution of higher quality products or services covered by the agency agreement, including market-specific investments as explained in paragraph 12 below, and those solely associated with the distribution of products or services that the agent distributes independently on its own behalf. This is the case, because in the scenarios presented so far to DG Competition, the agent undertakes a dual role in a market comprising differentiated products presenting objectively distinct characteristics and where there are otherwise no indicia that would suggest that other conditions for the sale of other products in the principal's product range may be affected. Conversely, in product markets comprising products not presenting objectively distinct characteristics, such delineation appears more difficult and there may therefore be a significant risk of the agent being influenced by the terms of the agency agreement, notably regarding the price setting, for the products it distributes independently.

11. Paragraphs 12-21 of the Vertical Guidelines provide guidance on the factors that define genuine agency agreements for the purposes of Article 101(1) TFEU. These factors derive from the case law of the Court[8]. As set out by the Court, the decisive factor for the purposes of determining whether an intermediary is an independent economic operator is to be found in the agreement concluded with the principal and, in particular, in the clauses of that agreement, implied or express, relating to the assumption of financial and commercial risks linked to sales of goods to third parties. The question of risk must be assessed on a case-by-case basis, taking account of the economic reality of the situation[9].

12. The Vertical Guidelines focus on three types of financial or commercial risk that are material to the definition of a genuine agency agreement, namely (i) contract-specific risks which are directly related to the contracts concluded and/or negotiated by the agent on behalf of the principal, such as the financing of stock; (ii) risks related to market-specific investments, which are investments specifically required for the type of activity for which the agent has been appointed by the principal; and (iii) risks related to other activities undertaken in the same product market, to the extent that the principal requires the agent to undertake such activities,

[8] See in particular the judgments in Case T-325/01, 15 September 2005, *Daimler Chrysler v. Commission*; Case C-217/05, 14 December 2006, *Confederación Espanola de Empresarios de Estaciones de Servicio v CEPSA* and Case C-279/06, 11 September 2008, *CEPSA Estaciones de Servicio SA v. LV Tobar e Hijos SL*.

[9] See Case C-217/05, 14 December 2006, *Confederación Espanola de Empresarios de Estaciones de Servicio v CEPSA*, paragraph 46.

not as an agent on behalf of the principal but for its own risk[10]. For the purposes of applying Article 101(1) TFEU, an agreement will be qualified as a genuine agency agreement if the agent bears no, or only insignificant, risks of the three aforementioned types. However, as set out in paragraph 15 of the Vertical Guidelines, "*risks that are related to the activity of providing agency services in general, such as the risk of the agent's income being dependent upon his success as an agent or general investments in for instance premises or personnel*" are not material to the assessment of whether an agreement constitutes a genuine agency agreement. Paragraph 16 of the Vertical Guidelines aims to provide more concrete guidance on these principles, by setting out examples of situations in which an agreement will generally be considered a genuine agency agreement.

13. Compliance with these requirements has to be assessed in a very strict manner to avoid a misuse of the agency concept in scenarios where the supplier does not actually become active at the retail level, taking all associated distribution decisions and assuming all related risks in accordance with the principles set out below, but rather establishes an easy way to control retail prices for those products that allow high resale margins. Since resale price maintenance is considered as a hardcore restriction under the VBER, the agency concept should not be misused by suppliers to circumvent the application of Article 101(1) TFEU.

Applicability of Article 101(1) TFEU to agency agreements with agents that act in a dual role for the same principal

14. As set out in paragraph 16(g) of the Vertical Guidelines, the existence of a genuine agency agreement is not *per se* incompatible with the agent also acting as an independent distributor within the same product market, provided that the principal fully reimburses the activities that it contractually requires the agent to engage in. That said, as explained in paragraph 9 above, this example concerns scenarios in which the distributor's main activity is the distribution of agency products on behalf of a principal, whereas the distributor is required to carry out independently only limited other activities.

15. Based on experience gathered by DG Competition so far, in all other scenarios of agents acting in a dual role, the agency agreement may only fall outside Article 101(1) TFEU if (i) the distributor is genuinely free to enter into the agency agreement (i.e. this is not *de facto* imposed by the principal through, for example, a threat to terminate or worsen the terms of the distribution relationship) and (ii) all relevant risks linked to the sale of goods covered by the agency agreement to third parties are borne by the principal, as explained in §§19-25 below, provided these activities and risks can be effectively delineated to avoid that risks and incentives associated to the distribution of services that the agent distributes independently on its own behalf may be affected.

16. The three types of financial or commercial risk that are material to the definition of an agency agreement, as set out in paragraph 15 of the Vertical Guidelines, should all be taken into account in the assessment. As set out in paragraph 12 above, the only investments that are

[10] See Case C-217/05, 14 December 2006, *Confederación Espanola de Empresarios de Estaciones de Servicio v CEPSA*, paragraph 50-62; Case C-279/06, 11 September 2008, *CEPSA Estaciones de Servicio SA v. LV Tobar e Hijos SL*, paragraphs 37-41.

not relevant to this assessment are those investments that are common to agency activities in general. This includes costs such as the renting of a shop or staff salaries, which can in principle be considered general investments in premises or personnel, as long as they can also be used for the sale of different goods unrelated to the agency agreement.

17. In situations where an undertaking acts in a dual role as agent and independent distributor for the same supplier, defining market-specific investments is of particular relevance. It should be noted that in a scenario where a supplier enters into an agency agreement with independent distributors that are already active on the relevant market, it is likely that many of the relevant costs will have already been incurred, thus raising questions about whether and to what extent the principal should cover such costs.

18. Market-specific investments are defined in paragraph 16 of the Vertical Guidelines as "*investments specifically required for the type of activity for which the agent has been appointed by the principal, i.e. which are required to enable the agent to conclude and/or negotiate this type of contract. Such investments are usually sunk, which means that upon leaving that particular field of activity the investment cannot be used for other activities or sold other than at a significant loss"*.

19. As set out in paragraph 14 of the Vertical Guidelines, where an undertaking on a downstream market acts in a dual role as genuine agent and independent distributor for the same supplier, market-specific investments should be understood as covering all investments necessary to enable an agent to negotiate or conclude contracts in the relevant market, including sunk investments that would be lost if the agent were to cease all activity in the relevant market (i.e. as agent or independent distributor). This includes, for example, investments in furnishing a shop or in training sales staff that are specifically required for selling products in the relevant market and that cannot be used commercially for activities in other product markets or only at a significant loss.

20. In a scenario where genuine agency agreements are entered into with existing independent distributors, it is DG Competition's current position that the fact that some of the market-specific investments may already have been incurred by the agent when acting as an independent distributor does not mean they do not have to be covered by the principal. In order for the agency agreement to fall outside the scope of Article 101(1) TFEU, all investments required for a genuine agent to negotiate or conclude contracts with third parties on the relevant market should be reimbursed, including market-specific investments, whether or not the agent is also acting as an independent distributor. To the extent that the relevant investments have already been depreciated (e.g. investments in activity-specific furniture), the reimbursement maybe adjusted proportionately. DG Competition proposes that in practice, to establish the level of reimbursement, the principal should consider the hypothetical situation of a distributor that is not yet active in the relevant market (either as agent or independent distributor) in order to assess which investments are relevant to the type of activity for which the genuine agent will be appointed.

21. As explained in paragraph 15 of the Vertical Guidelines, market-specific investments, which have to be covered by the principal for the agency agreement to be considered genuine, have to be distinguished from investments related to the provision of agency services in general,

which do not need to be covered by the principal. That said, some investments are likely to be partly common to the provision of agency services in general and partly specifically required for the type of activity for which the genuine agent has been appointed by the principal. This is the case, for example, for investments in a website or general advertising for a shop rather than the principal's brand or specific products. DG Competition proposes that for this type of investments, the principal should cover a share of the costs, as they are likely to be (at least in part) market-specific.

22. It is DG Competition's current position that the only market-specific investments that the principal would not have to cover would be those that relate exclusively to the sale of differentiated products in the same product market that are not covered by the agency agreement and distributed independently, by contrast to market-specific investments needed to operate in the relevant product market that the principal would have to cover in all cases. This is because the agent would not incur the market-specific costs corresponding to these differentiated products if it did not also act as an independent distributor for those products in addition to the products it distributes as an agent, provided that it can operate on the relevant market without selling the former.

The following example illustrates the current position of DG Competition on how costs could be allocated in practice in a case of a distributor that also acts as agent for certain products for the same supplier.

One could consider the hypothetical scenario of a dual role agent, selling products A, B and C. Products A and B belong to the same product market, which comprises differentiated products presenting objectively different characteristics. Product C belongs to a different product market.

A supplier of product B generally distributes its products using independent distributors. However, for the distribution of a particular type of the same product, namely product A which features a new functionality, it wishes to use an agency agreement, which it offers to its existing independent distributors in the same product market without *de iure* or *de facto* requiring them to enter into this agreement.

For the agency agreement not to fall in the scope of Article 101(1) TFEU (and to meet the conditions of paragraphs 12 to 18 of the Vertical Guidelines to be considered as a genuine agency agreement), the principal has to cover all relevant investments to the activity of selling each of products A and B (and not only A products) as they belong to the same product market. For example, all costs incurred to adapt or furnish a shop in order to display and sell products A and B are likely to be market-specific. Similarly, the costs of training personnel in order to sell products A and B and costs related to specific storage equipment, which may be needed for products A and B, are also likely to be market-specific. These relevant investments, which would normally be required for an agent to enter the market and start selling products A and B, should be borne by the principal even if the specific agent is already established on that market as an independent distributor.

However, the principal would not have to cover investments for the sale of product C, which does not belong to the same product market as products A and B. Moreover, in case the sale of product B requires specific investments that are not necessary for the sale of product A (e.g. dedicated furniture or staff training), such investments would not be relevant and would therefore not have to be covered by the principal, provided that a distributor can operate on the relevant market comprising products A and B by selling only product A.

As regards advertising, investments in advertising for the agent's shop as such (instead of advertising specific to product A) would benefit both the agent's shop in general as well as the sales of products A, B and C, while only product A is sold under the agency agreement. These costs would therefore be partly relevant for the assessment of the agency agreement, to the extent they relate to the sale of product A which is sold under the agency agreement, while they are also relevant to the general activity of selling products A and B. The cost of an advertising campaign relating exclusively to products B or C, however, would not be relevant and would therefore not have to be covered by the principal, provided that a distributor can operate on the relevant market selling only product A.

The same principles apply to investments in a website or an online store, since part of these investments would not be relevant, as they would have to be made irrespective of the products sold under the agency agreement. Therefore, general investments in the design of a website would not have to be reimbursed, insofar as the website structure itself could be used to sell products other than those belonging to the relevant product market (e.g. C products or, more generally, products other than A and B). However, investments related to the activity of selling or advertising products in the relevant product market (i.e. both products A and B) on the website would be relevant. Therefore, depending on the level of investment required to advertise and sell A and B products on the website, the principal would have to cover part of the costs of setting up the website or the online store. Any specific investments for advertising or selling product B only would not have to be covered, provided that a distributor can operate on the relevant market selling only product A.

Methods of financing the risks related to the activities covered by the agency agreement

23. Another issue raised by stakeholders concerns the method for reimbursing the relevant costs incurred by the agent. Considering that there may be different ways in which an agent can be reimbursed, no particular method is required for an agreement to qualify as a genuine agency agreement, provided that the relevant costs are fully covered by the principal. For example, a principal may choose to reimburse the precise costs incurred. A principal may also choose to cover these costs by way of a fixed lump sum or by paying to the agent a share (fixed percentage) of the revenues from products sold under the agency agreement. All of these reimbursement methods are in principle acceptable, especially in situations where a principal may work with a large number of agents, as they may reduce the administrative burden for the principal and the agents concerned. However, DG Competition proposes that such methods of reimbursement should be designed in a way that ensures that they always cover all the relevant costs, so that the genuine agent bears no, or only insignificant, risks of the three types of financial or commercial risk set out in paragraph 12 above. This may require a reimbursement system that allows the agent to easily declare and request the reimbursement of any costs that exceed the lump sum or fixed percentage. It may also require the principal to monitor and review changes to the relevant costs and to adapt the lump sum or fixed percentage at regular intervals in order to account for any significant changes in the level of costs in a way that does not create a burden for the agent. Such a system would ensure that the genuine agent is in practice reimbursed for all relevant costs.

24. In addition, DG Competition proposes that when setting the lump sum or fixed percentage, the principal should ensure that it adequately reflects any cost variation that may exist between genuine agents operating in different Member States, or between genuine agents operating under different business models (e.g. agents that only operate a brick-and-mortar store, agents that only operate online without being an online platform, or hybrid agents operating in both ways).

25. In particular, DG Competition's current position is that where the relevant costs are reimbursed by way of a percentage of the price of the product sold under the agency agreement, the principal should also take into account that the genuine agent may incur relevant market-specific investments even where it makes no sales for a certain period of time. Such a reimbursement system would therefore need to include a method for calculating and reimbursing these costs in case the agent does not make any sales, even if only for a short period of time.

Market monitoring

26. As indicated in paragraphs 7, 8, and 10 above, a model whereby an undertaking active on a downstream market acts both as an agent and as an independent distributor within the same product market for the same supplier may raise competition concerns as regards the incentives of the agent/independent distributor or the possible impact on sales conditions and in particular the pricing of the products sold as part of the independent activity. In view of this, DG Competition will carefully monitor developments in this area, based on market information from stakeholders and national competition authorities, and may revise the principles proposed in this working paper, if there are indications that the implementation of a dual role for agents in the same product market risks giving rise to competition concerns. In addition, this working paper is without prejudice both to the outcome of the ongoing review of the VBER and the Vertical Guidelines, and to DG Competition undertaking investigations in cases of agency agreements concerning dual role agents that do not follow the principles proposed in this working paper or for which there are indications that the agency concept is misused to circumvent the application of Article 101(1) TFEU.

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