International Distribution Institute

COMMENTS OF THE INTERNATIONAL DISTRIBUTION INSTITUTE ON THE PRELIMINARY REPORT ON THE E-COMMERCE SECTOR INQUIRY

The International Distribution Institute deals since several years with issues regarding cross-border distribution through its website, its model contracts, country reports, etc. IDI organizes a yearly conference where companies and lawyers involved in international distribution discuss topical issues arising in this field (the subject matter of the 2016 yearly conference was "Selling on the Internet").

IDI has consulted its members on the issues arising out of the Preliminary Report. This paper deals with some of the main preoccupations raised in this context by companies engaged in distribution within the EU and their consultants.

1. General considerations

IDI welcomes the decision by the Commission to ascertain the actual market situation and current practices regarding on-line sales before deciding how to promote e-commerce and in particular how to approach business practices which may affect the development of cross-border internet sales.

It is obvious that the promotion of on-line competition, which in principle favours consumers, may conflict with the efficient management of distribution networks.

Companies engaged in distribution within the EU must defend themselves and their networks against aggressive practices which are made possible by Internet and which may disrupt the existing distribution systems. On one side, the off-line channel, which still plays an essential role in consideration of the importance of the services it offers to the consumers, must be safeguarded. On the other side, manufacturers who invest in their brand and corporate image must be able to defend themselves against practices on the Internet which may negatively affect their image/reputation and market positioning.

It is therefore important that, when assessing possible restrictive business practices, which may be seen as an obstacle to the development of e-commerce, due regard is given to the need to warrant the efficient functioning of distribution networks, which is and remains of substantial importance for consumers.

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2. Use of terms which may give rise to misunderstandings

We would like to draw the attention on some notions referred to in the Preliminary Report which may give rise to misunderstandings.

When the Preliminary report refers to **retailers**, it is not always clear whether this category includes the producers, when they sell directly to consumers through their website.

If this were the case, statements regarding restrictions imposed on retailers by manufacturers should regard only retailers who resell goods supplied to them by others, with the exclusion of the manufacturers who sell their own goods directly to consumers through their website. However, the Preliminary Report does not seem to make this distinction.

Another term which may create confusion is "**marketplace**", which covers as well the site on which a retailer or producer can be hosted as the case where the marketplace buys and resells the goods. These situations must be considered differently. For instance, when a manufacturer restricts the right of a retailer bound by a selective distribution agreement to access marketplaces, one should consider differently the direct sale by the retailer through the marketplace and the case of a resale by the marketplace, which would amount to a sale to an unauthorized reseller.

3. Selective distribution

Before approaching this very important subject-matter, it is important to underline that the EU market for consumer goods is not highly concentrated and that consequently all possible restrictive agreements fall under the block exemption regulation 330/2010. We will therefore consider possible restrictive practices only in the context of the BER, without making reference to the more restrictive principles developed in the past and still applicable to agreements not covered by the BER.

Selective distribution has become a necessary tool for producers who wish to make sure that their products are proposed and sold to consumers in the most appropriate way. This is particularly the case for certain kinds of products, like products requiring advice at the point of sale, luxury goods which need to preserve brand image/reputation, etc. But, in consideration of the growing facility for third parties to interfere with the existing networks through Internet, the creation of a closed network of retailers bound contractually to the supplier is becoming more and more a necessary option for manufacturers, also for a wider range of products.

The Commission seems to fear that extending the range of products which may be admitted to selective distribution could give rise to abuses, but this position is not justified. In fact, it should be considered that the requirements imposed by the BER (such as in particular the right to active sales to consumers without territorial limitations) should be sufficient to exclude the risk of abuses. It is important to consider that the freedom to apply selective distribution to whatever type of goods, introduced since 1999 by regulation 2790/1999, has not given rise to particular problems.

To our knowledge, in all these years the Commission has never made use of the possibility of withdrawing the benefit of the block exemption.

Furthermore, introducing limitations to the clear rules of regulation 330/2010, which do not limit the kind of products for which selective distribution may be uses, would create uncertainty and contradict the need for certainty which is the main purpose of the block exemption.

In more general terms, it would be inappropriate to try to use the e-commerce inquiry for the purpose of reviving prohibitions which were abandoned (for agreements under the 30% threshold) with the enactment of regulation 2790/1999.

This implies that manufacturers should be free to decide the criteria for admission to the to the network (since event quantitative selection is exempted under the BER), like excluding "discount" retailers, requiring a brick and mortar shop, banning the sale through marketplaces.

4. Marketplace bans

We welcome the permissive line of the Commission regarding provisions banning resellers from selling through marketplaces. This is particularly important within selective distribution, in consideration of the need to enforce the manufacturer's choice to have its goods are sold at the retail level in compliance with its quality and marketing policy. The freedom of the manufacturer to decide the most appropriate marketing policies (which necessarily include the prohibition of inappropriate sales channels) is a substantial means for promoting intra-brand competition which should be favoured by the competition authorities.

Since even an absolute prohibition to sell via marketplaces does not amount to a prohibition to sell on the Internet, the exclusion of certain types of marketplaces supported by objective reasons, should certainly be considered as not being anti-competitive.

Without prejudice to the legitimate refusal to allow retailers to sell via marketplaces on the basis of brand image and reputational reasons, luxury brands emphasize that their reluctance to deal with marketplaces is also based on the need to fight against counterfeit trade.

Although the majority (*i.e.*, slightly more than 60%) of marketplaces declared to have specific tools in place providing third parties with the possibility to report counterfeit items and request their take down, it appears that the tools and mechanisms actually in place to combat the trade in counterfeit goods are not appropriate to ensure adequate protection to intellectual property right owners.

Until Europe adopts a clear legislative framework and courts provide univocally direction on this matter (and until marketplaces exercise a more effective control prior to the listing of the product on their platforms) brand owners – especially luxury brand owners – are entitled to keep a cautious approach and therefore to lawfully refuse to have their products traded via marketplaces.

5. Resale pricing

Internet has dramatically increased the possibility to propose aggressive prices which can provoke irreparable damages to a distribution network and to the brand image of the manufacturer.

Manufacturers who respect the prohibition of resale price maintenance, and leave the retailers free to determine their prices, can in no way accept forms of aggressive pricing which go beyond certain limits, if the correct functioning of their distribution network is put into danger.

They will have recourse to recommended pricing with the expectation that the retailers will understand that their pricing policy should comply with certain general criteria, in order not to disrupt the existing distribution network.

This result can be obtained without requiring the observance of specific minimum prices, like the provisions of a communication to resellers accepted by the Italian competition authority in the Enervit case (Case n. 25021 of 09/07/2014) worded as follows:

> Gli ingenti investimenti profusi in ricerca e sviluppo e in politiche di marketing a sostegno del valore intrinseco dei nostri prodotti hanno consentito la diffusione e il consolidamento dei marchi Enervit, Gymline, EnerZona ed Enervit Protein che oggi sono universalmente riconosciuti come sinonimo di qualità e sicurezza alimentare. Le scelte di posizione di prezzo riflettono i valori della nostra azienda e la qualità dei nostri prodotti.
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> Ciascun rivenditore è libero di determinare i prezzi al pubblico e i relativi sconti in totale autonomia nel rispetto dell'immagine e del valore dei marchi di Enervit."
>
> The huge investments made for research and development and marketing to sustain the real value of our products have made it possible to promote and reinforce the brands Enervit, Gymline, EnerZona ed Enervit Protein, which are at present recognized to be the expression of quality and food safety. Their price positioning reflects the value of our company and the quality of our products.
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> Each reseller is free to fix the resale prices and respective discounts in total autonomy, while respecting the image and value of the Enervit brands.

While it is obvious that manufacturers may not force resellers to respect a recommended price, they should be entitled to require the respect of a reasonable price range, coherent with the supplier's brand image and price positioning. In the absence of this type of flexibility, it would be impossible for manufacturers to establish any reasonable pricing policy, which would result in a strong incentive towards vertical integration.

The Preliminary report considers the importance of recommended retail prices for the positioning of the brand (§ 514) and the need to consider the estimated price level when designing and manufacturing the product (§ 515). If manufacturers have the right to pursue a certain pricing policy and to recommend prices, they must also be able to incentivate in some way their recommendations, which would otherwise be useless.

A further critical issue regards price advertising. Advertising aggressive prices on the Internet can disrupt the operation of an established distribution network, without long-term advantages for consumers. The Commission should re-examine its position on Minimum Advertised Price (MAP), as expressed in its reply to the Petition of 25-11-2015 to the European Parliament n. 2383/2014, with respect to situations where the MAP would express a minimum price at the bottom of a range of "reasonable" prices.

6. Adwords - Restrictions to bid only on certain positions

With respect to restrictions to sell or advertise online (Preliminary Report, §§ 574 – 580), the Commission states that allowing retailers to bid only on certain positions in order to get a preferential listing on the search engines paid referencing service may raise concerns under Article 101 TFUE. Basically, the Commission's theory is based on the observation that search engines are powerful tools for attracting customers to the retailers' website and therefore any limitation to bid for a preferential position would restrict retailers' ability to attract online customers.

However, following the reasoning applied by the Court of Justice in *Pierre Fabre* (C-439/09 *Pierre Fabre Dermo – Cosmétique SAS* , judgement of 13 October 2011) and in line with the arguments put forward by the Commission in relation to the marketplace ban, such a limitation would only represent a violation of Article 101(1) TFUE when it amounts to a complete ban to use the Internet channel. It seems very hardly arguable that a limitation of the retailer's ability to achieve a prominent position on search engines' sponsored areas could correspond to a *de facto* prohibition to sell online.

Indeed, as the Commission stated in the Preliminary Report, these clauses concern the "*question of how the distributor can sell the products over the internet and do not have the object to restrict where or to whom distributors can sell the products*" (§ 472, emphasis added). The search engines' sponsored areas do not in fact represent the only way to attract customers to the retailers' website as there are many other ways through which traffic can be directed to a retailer's website (e.g., through direct URL, online marketplaces, price comparison tools, and mobile apps).

It is also worth noting that in the Preliminary Report the Commission expressly stated that restrictions on the ability of retailers to use the manufacturer's brand name in the retailer's own domain name would help avoiding confusion with the manufacturer's website; meaning that they would not be regarded as a restriction of competition under Article 101 TFUE.

In fact, consumers should not be misled when searching for products online and the brand's image should not be negatively impacted. Intellectual property right owners should be therefore entitled to regulate the use of search engines' sponsored areas in order to avoid any consumers' confusion.

The so called 'bidding price war' on Google has the effect of perversely increasing the prices for securing the best positions. Beside the brand-owners, that are forced to pay incredible amounts of fees to purchase Adwords which strictly comprise their own intellectual property, such war is damaging also smaller retailers that may not afford to pay such high prices. Moreover, linking online brand presence solely with the ability (or willingness) to pay the highest amount for a Google Adword has the potential to significantly distort search results, leading consumers to websites that might not be of greatest relevance to them or of greatest service quality or range.

Having said that, considering that these are recent issues on which the Commission has not yet taken a position that could be considered for the purpose of conducting a compliance exercise, there is a great need for clear guidelines that the Commission may provide by analyzing more in depth said alleged restrictions in the conclusive report of the Sector Inquiry.

It is also worth investigating whether there might potentially be circumstances where certain restrictions on purchasing trademark-protected key words (including by authorized retailers in a selective distribution system) would be objectively justifiable. Such restrictions encourage the significant investments made by manufacturers and brand-owners in developing their intellectual property and brand reputation, together with investments in enhancing the quality and innovation of their products and design. An unfettered ability by resellers to purchase trademarked terms might potentially discourage such investments as well as mislead consumers as to the rightful brand-owner, thus undermining the protections afforded by intellectual property laws in the EU.