

# **COMMISSION “PRELIMINARY REPORT ON THE E-COMMERCE SECTOR INQUIRY”**

## **- PRELIMINARY OPINION OF INDEPENDENT RETAIL EUROPE -**

**9 NOVEMBER 2016**



## PRELIMINARY COMMENTS OF INDEPENDENT RETAIL EUROPE ON THE COMMISSION STAFF WORKING DOCUMENT “PRELIMINARY REPORT ON THE E-COMMERCE SECTOR INQUIRY”

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### The role of selective distribution

The sector inquiry classifies selective distribution as a system whereby ‘*distributors are selected on the basis of specific criteria, set out in the distribution agreement.*’ The sector inquiry recognises that selective distribution has an important role to play in commercial relationships. However it raises suspicions that selective distribution contracts are being abused by manufacturers wishing to ban certain online retailers/platforms from selling a product.

Some evidence points to the fact that selective distribution is being used to react to the growth of e-commerce as “changes to selective distribution systems” is reported as one of the most frequent manufacturer reactions to the rise of e-commerce.

The criticisms by the retailers are most prominent from the online/offline operators who accuse manufacturers of setting criteria that cannot feasibly be met if selling a product online. Manufacturers respond to these allegations by saying they require high quality distribution to ensure they remain competitive as this helps to maintain their brand image; have quality pre and post sales service and improve the overall shopping experience for consumers.

Clothing, cosmetics and consumer electronics are the areas where selective distribution systems are most common.

### Our comments:

- Selective distribution must be maintained as a valid distribution system and not unfairly stigmatised. Those retailers (as opposed to 3<sup>rd</sup> party platforms operating under their own name) who meet the selective criteria should in principle be allowed to sell the product.
- The European Commission should be more comprehensive when stressing some of the positive aspects of selective distribution. For example, goods distributed through selective distribution play an important differentiating role for our members when it comes to the assortment, particularly in non-food assortments.
- It is popular with consumers as it allows expert staff to give informed advice on specialist goods such as skis, specialist footwear, sound systems etc.
- It maintains the value and quality of brands due to the sales environment and high service levels both on- and offline.
- Selective distribution helps to level the playing field for online and offline sales as EU rules already determine that criteria for on- and offline sales should be equivalent.
- In principle, the head of a distribution network should be free to choose in which sales channel it wishes its product to be distributed and under what sales strategy. Even if the product is not a luxury product, or a highly technical product that justifies a selective approach with highly qualified staff etc. it should be possible to organise online sales according to its own commercial strategy.
- In relation to selective distribution, an additional issue is how selective criteria link into rebate packages. As regards on and offline sales agreements, certain aspects of remuneration, such as rebates, are treated differently dependent on the sales channel. For instance, offline retailers can under interpretations of existing law (such as national interpretations paragraph 52 (d) of the Guidelines on Vertical Restraints) only be remunerated by means of a lump sum rebate rather than performance related rebates to prevent accusations of dual pricing. Remuneration types, such as

rebate related agreements, based on sales performance, by contrast, appear to be incompatible with European law according to the interpretations given to it by for example the *Bundeskartellamt* (1). We are of the opinion that retailers and suppliers should be free to negotiate remuneration such as rebates in each channel/purchasing agreement as they see fit.

### Resale Price Maintenance

The European Commission has assessed the pricing strategies of retailers online. One potential worry is over the transparency of prices online and the tracking software used to monitor competitors' prices. This can facilitate collusion between retailers on prices or it can lead to a race to the bottom in terms of retail prices. In order to prevent the race to the bottom, manufacturers and retailers could illegally agree on minimum retail prices, an anti-competitive behaviour. This behaviour artificially protects the wholesale price paid to manufacturers and protects the margin made at retail level. The Commission is concerned that legally allowed recommended prices may in reality be an illegal minimum retail price as evidence suggests that manufacturers track retail prices in specific markets closely (with the implication being that once price deviations are found there may be punishment).

#### Our comments:

- We believe that vertical collusion in the supply chain on prices is extremely rare. Equally, we believe that horizontal collusion between retailers is extremely rare.
- Price transparency is likely to lead to lower prices. This has immediate consumer welfare benefits in terms of generating greater consumer surplus. However, it can have unintended consequences such as reducing the value of branded goods in the mind of a consumer. Retailers try to maintain the value of brands in different ways, such as through in-store and at-home services, including more qualified staff, levels of advice in the point of sale etc. Lower prices are likely to lead to cut-backs in these additional services that are of high consumer benefit.

As regards resale price maintenance within groups of independent retailers, we fully endorse the following extract on this issue **taken from the Commission's own report of the SME sub group (2) of the Commission's High Level Group on Retail Competitiveness:**

- *Independent retailers working together in specialist structures are heavily affected by the interpretation of competition rules. These include guidance provided at the EU level in the Regulation on Vertical Restraints (Commission Regulation 330/2010); the linked Vertical Guidelines (2010/C 130/01); and the Horizontal Competition Guidelines (2011/C 11/01).*
- *These documents limit, in practice, how independent retailers can interact within their specialist group structures. Limits are notably placed on information exchanges on pricing, marketing, branding etc.*
- *The possibility of pricing agreements (resale price maintenance [RPM]) within such groups particularly in the context of e-commerce are an essential necessity to ensure the competitiveness of these groups in future and enhance competition in the e-commerce market. When independent retailers, operating in a group under a common brand, do not have a unified pricing policy, they are not able to develop an efficient online service and a uniform brand image. This creates a*

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(1) See amongst other Dornbracht, Gardena, [http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2013/B05-144-13.pdf?\\_\\_blob=publicationFile&v=3](http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2013/B05-144-13.pdf?__blob=publicationFile&v=3) and Dornbracht [http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2011/B5-100-10.pdf?\\_\\_blob=publicationFile&v=4](http://www.bundeskartellamt.de/SharedDocs/Entscheidung/DE/Fallberichte/Kartellverbot/2011/B5-100-10.pdf?__blob=publicationFile&v=4) as well as undertakings by Bosch-Siemens and Lego

(2) Report of the SME sub group <http://ec.europa.eu/DocsRoom/documents/11766/attachments/4/translations/en/renditions/native>

*competitive disadvantage for independent retail SMEs compared to integrated chains, which use common pricing to develop their brand image. For example, price can convey quality or value, as an image, depending on the image a brand wishes to project.*

- *Moreover, when independent retailers, who are part of a group, do not have access to a harmonised web portal, their search ranking e.g. in Google is drastically reduced. This is because, despite the independent retailers selling the same products, Google doesn't recognize their content as unique and so the combined purchases from the independent retailers belonging to the same grouping are not used to determine the search ranking. This has negative sales implications and a huge business impact.*
- *Although there are groups of independent retailers who have tried to build up multichannel-concepts under a single brand, the lack of the possibility to set prices makes it more difficult to maintain a consistent brand-image and online appearance. For example many independent retailers cooperating in groups have not been able to set up a common consumer facing e-commerce platform due to restrictions on using RPM. Instead, in many cases, each independent retailer (even when part of a wider group) will have his own web offering. This leads to hundreds, if not thousands of different websites of independent retail group members, which makes it burdensome and complex for a consumer to search independent retailer's e-commerce sites and to shop on-line which dilutes the brand image of a group and weakens a brand in the mind of the consumer. It also prevents efficiencies of scale (costs are carried and operation of IT-system is done by each independent retailer, SME, etc.), as the retailers cannot join forces with their peers in the same retailer grouping to establish a common e-commerce portal. An independent retailer faces extreme difficulties to build up and maintain an efficient and competitive e-commerce service of a considerable number of articles him/her self. However, by using a common 'group' web portal, this barrier is overcome and independent retailers can offer the omni-channel shopping experience, demanded by modern consumers.*
- *Intra-group RPM in this situation would benefit consumers by boosting inter-brand competition as efficient cooperation in groups (also in the sphere of e-commerce) is the only way for independent retailers to compete with integrated chains. Indeed, it is in the consumer interest to have a strong 'independent' sector and therefore a diverse retail sector. To aid this, there should be a level playing field for groups of independent retailers and integrated chain business models to compete on.*
- *The benefits of the efficiencies created by RPM within a group of independent retailers are for the consumers in the form of more choice and lower prices.*
- *It is indispensable for groups of independent retailers to find ways of carrying out efficient e-commerce operations as omni channel retail offerings are nowadays standard consumer expectations. Allowing RPM within groups of independent retailers should therefore be a priority measure enabling independent retailers to compete online.*
- *This can be done by adding new RPM provisions to the existing vertical competition guidelines in order to take into account new market developments e.g. the rise of e-commerce and digital customer communication or in the short-term by providing specific guidance on these issues.*
- *It could be argued that groups of independent retailers could use the exemption from certain categories of agreements from competition law, contained in Article 101(3) of the Treaty on the Functioning of the European Union, to legally use RPM agreements. However, this is considered unrealistic by the independent retailers. Using a general treaty exemption to prove efficiency gains in each case is far too burdensome and indeed legally uncertain for each retail SME, or group, to do.*

In conclusion, there are various aspects to resale price maintenance, including certain benefits that are very important for the future development of a healthy e-commerce market.

### Price comparison tools

The European Commission confirms that the ability to be found by search engines and price comparison websites is a key factor to effectively compete with other retailers. This confirms the rationale behind a group of independent retailers having one online portal, with a common price that generates sufficient combined sales volumes to be picked up by search engines and is able to be listed on popular comparison tools.

#### *Our comments:*

- Price comparison tools should include data other than prices in their displays e.g. services provided. Our members compete by providing better services; not just competing on price.
- Price comparison portals require a new retail mind-set. In view of the improved product information available to consumers, retailers and manufacturers need to ensure high conversion rates (operational success rates) by providing personalised, customer-focused information and follow-up services. This, in turn, necessitates new training concepts (initial and further training) in retail.
- This situation could be seen as an opportunity: customer satisfaction can be enhanced by means of new, innovative approaches.

### 3<sup>rd</sup> party platforms/market places

The inquiry describes the growth in market places over the last 15 to 20 years as an important sales channel for online sales. They are seen as particularly important to SME retailers who can use them to access a wide range of customers with relatively low start-up costs. The main issues are around the relationship between marketplaces and manufacturers e.g. prohibition to sell via 3<sup>rd</sup> party platforms or equivalent measures (e.g. selective distribution agreements with quality criteria that cannot be attained by a retailer selling on a 3<sup>rd</sup> party platform) imposed by manufacturers who do not want products listed on market places as they consider it would devalue the brand.

The Commission stresses that market place bans are not hardcore competition restrictions. EU rules allow manufacturers to ban direct sales via marketplaces which only carry the name and logo of the marketplace operator.

#### *Our comments:*

- The organiser of the distribution network which uses a common branding (such as a group of independent retailers) should be allowed to require a physical point of sale. This is a conscious strategic decision used to conserve the human touch for a consumer and maintain a close link to the consumer. This is a natural strategy in a group of independent retailers operating under a common branding. An independent retailer benefits from the group's branding and wider network of physical stores owned by other independent retailers. Requiring a physical store prevents free riding (by an independent retailer operating only online) on the investments in the brand and store network that have been made through physical stores developed by independent retailers offline. For the same reason, a ban on the use of third party platforms in a group of independent retailer's online rules should be allowed, if a group of independent retailers chooses such a commercial strategy. After all, the group's strategy is determined by the wishes of its independent retailer members.
- Furthermore, the necessity to have a physical store does not stop a product from being sold online, it merely obliges the independent retailer to have a multi-channel strategy which can only be more favourable to the consumer: the consumer has all the benefits of an online store yet a closeness to the

retailer is ensured; a physical point of contact for advice, or resolution of problems exists; and it is possible to pick up or return products easily.

- Removing restrictions that have beneficial consumer effects such as the requirement to have a physical store, obligations not to sell on platforms or distribution agreements such as selective distribution would have serious consequences such as the replacement of multi-channel retailers that offer great consumer convenience, with pure online players with the attendant negative consumer benefits (broadly a lack of consumer proximity i.e. lack of help and advice if it is needed; lack of sales innovations due to lack of competing sales channels; ultimately higher prices, less consumer choice and less process innovation as e-commerce retail becomes increasingly concentrated with few yet high market share players. Other social aspects should also be taken into account such as urban decay and less investment in local communities as profits made by pure players are moved offshore.
- A question the sector inquiry fails to address is the extent to which limits on distribution channels (such as platform bans) might lead to stronger brand images, for the manufacturers and the retailers, and better, more customer-focused services as well as more sustainable supply chains.

The sector inquiry has missed a key part of the e-commerce debate in its research:

- There is no apparent mention or research into the extent of the free-riding of 3<sup>rd</sup> party platforms on the proprietary data generated by marketplace users (retailers) where platforms play a role both as marketplace and retailer. For us, this is one of the major concerns with 3<sup>rd</sup> party platforms. In addition, the behaviour of platforms in pushing higher margin items to consumers (which may be to their detriment if the same product is available more cheaply (or at the same price) from a different seller on the platform with less margin going to the 3<sup>rd</sup> party platform) has not been looked at.
- There is no apparent investigation into the lack of a taxation level playing field when it comes to multi-channel retailers competing with 3<sup>rd</sup> party platforms acting as retailers. The current uneven playing field gives 3<sup>rd</sup> party platforms (and other pure e-commerce players) paying negligible levels of corporation tax an unfair competitive advantage over multi-channel retailers who pay corporation tax where the economic activity takes place.
- There is no apparent investigation into the uneven regulatory playing field whereby multichannel retailers are liable for waste take back (e.g. for waste electrical and electronic equipment, batteries etc.) whereas platforms (acting as retailers) and pure online retailers do not respect these obligations.
- There is no apparent investigation into the uneven regulatory playing field whereby multi-channel retailers are responsible for the safety and legal compliance of products sold in their stores and online, whereas platforms are not. This could be considered a form of free riding. The European Commission should evaluate the role and responsibilities of platforms. For those who are retailers, they should be subject to the usual retailer responsibilities e.g. arising out of product safety and waste legislation. If they are not retailers, yet have some hybrid role, adequate responsibilities matching their supply chain role should be developed to ensure a level regulatory playing field. In any case, we disagree with the suggestion put forward by platforms that they merely are equivalent to shopping centres. Shopping centres have vastly different remuneration policies; little or no trade in/use of data; no logistics obligations etc.
- For a true retail level playing field to exist in the future and for the e-commerce sector inquiry to be exhaustive, the above mentioned issues should be examined to prevent marketplaces profiting from unfair competitive advantages that place their multi-channel competitors in a disadvantageous position, ultimately leading to market exists; higher levels of concentration in e-commerce markets, reduced e-commerce innovation and overall reductions in consumer welfare, not least through future price rises as competitive pressures are reduced.

### Role of manufacturers as competitor and supplier

The sector inquiry identifies that over the last ten years many manufacturers have opened their own online shops to reap the benefits of online sales and better control distribution. This is notably the case in cosmetics and healthcare.

#### *Our comments:*

- The sector inquiry does not scrutinise potential conflicts of interest due to the role of manufacturers as both a competitor and supplier of retailers.
- Potential conflicts should be evaluated by DG Competition. For example, to what extent do manufacturers use/free ride on retailer generated sales data/trends/pricing/insights to, for example, develop new products that are then potentially not made available to retailers to sell? This is particularly important in product categories where suppliers are the 'dominant' party in the supply chain such as sportswear, electronics, and cosmetics.
- This distribution trend could have potentially anti-competitive consequences:
  - o Today, specialised offline retailers, due to the rapid growth of e-commerce, are struggling to remain competitive. More than ever, they depend on mutually beneficial relationships with manufacturers. This makes it regrettable that sales-based rewards on the part of suppliers are considered in some EU jurisdictions as inadmissible under current competition law, being considered a controlling, and thus illegal, intervention in distribution. It should be kept in mind that buying decisions are not based on price alone. In-store advice, staff expertise and the overall shopping experience are important factors as well; sales-based remuneration can help to promote this.
  - o When it comes to agreements between retailers and manufacturers, all aspects relevant to rewarding retail performance should thus receive due recognition. Remuneration systems that are entirely independent of sales performance have proven highly impractical in a retail context. At this point, requirements under competition law have indeed become so complex that manufacturers are no longer able or willing to meet them. More and more manufacturers have thus been induced to expand vertically, setting up their own sales outlets.

- ➔ **Overall we believe that the sector inquiry has the potential to show important trends in e-commerce. Despite some good analysis, several important issues have been overlooked. We hope that you find our contribution useful in this regard and we remain at your disposal to provide further input and clarifications.**
- ➔ **We expect to refine our preliminary position as the sector inquiry results are finalised and their implications become clearer over time.**

Established in 1963, **Independent Retail Europe** (formerly UGAL – the Union of groups of independent retailers of Europe) is the European association that acts as an umbrella organisation for the main groups of independent retailers in the food and non-food sectors.

*Independent Retail Europe represents retail groups characterised by the provision of a support network to independent SME retail entrepreneurs; joint purchasing of goods and services to attain efficiencies and economies of scale, as well as respect for the independent character of the individual retailer.*

*Our members are groups of independent retailers, associations representing them as well as wider service organizations built to support independent retailers.*

*Independent Retail Europe represents 23 groups and their 367,739 independent retailers, who manage more than 574.644 sales outlets, with a combined retail turnover of more than 809 billion euros and generating a combined wholesale turnover of more than 317 billion euros. This represents a total employment of more than 5.886.759 persons.*

More information about Independent Retail Europe under [www.independentretaileurope.eu](http://www.independentretaileurope.eu)