

Award in Competition Law

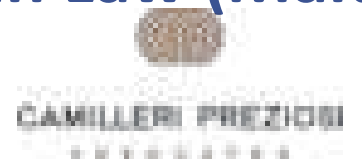
Lecture Title: Article 101 TFEU & Vertical Agreement

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Diploma in Law (Malta)



Recap: What does Article 101 TFEU cover?

EU Comp. law applies to anti-competitive agreements or business practices between:

- competitors (**horizontal agreements**) and/or
- Trading parties at different levels of the distribution chain(**vertical agreements**) (NB not consumers)

The TEXT of Article 101(1) READS “all [(**horizontal**) or **vertical**] agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market.”

1. An agreement (decision or concerted practice) between two or more
2. Undertakings (an economic activity)
3. Which has the “*object*” or “*effect*” of restricting or preventing competition
4. Having an effect on trade between MS (jurisdictional element for application of TFEU)

Competition Element: The Concept of Object/Effect

- The words "object" or "effect" are to be read disjunctively. It is, therefore, sufficient that an agreement has either an "object" or an "effect" that is anti-competitive
- By Object: "certain forms of collusion between undertakings can be regarded, by their very nature, as being injurious to the proper functioning of normal competition." : it is not necessary for the authority or the court to prove that the restriction had anti-competitive effects.
- For "by object" agreements regard must be had inter alia to the content of its provisions, the objectives it seeks to attain and the economic and legal context of which it forms part"
- The former EU DG for Competition Alexander Italianer has stated:

"Drunk driving is always illegal, because all our experience tells us that it is extremely likely to cause harm. The risk of harm is sufficiently great to warrant an outright prohibition, rather than judging infringements on a case by case analysis."



Competition Element: The Concept of Object/Effect

- On the other hand, where the analysis of the object of the agreement does not reveal an obvious anti-competitive objective, the next question is whether it restricts competition by effect.
- Classification: “non per-se” – not necessarily harmful to competition, their effect depends on particular circumstances as the nature of the agreement and market conditions
- This means that, for an agreement to have restrictive effects on competition within the meaning of Article 101(1) it must have, or at least be likely to have, an appreciable adverse impact on at least one of the parameters of competition on the market, such as price, output, product quality, product variety or innovation.
- Because: under certain conditions, agreements are likely to help realise efficiencies and the entry of new markets in a way which may offset possible negative effects. In general, vertical restraints will be viewed more favourably if they are of limited duration and assist in the introduction of new and complex products or the protection of specific investments.



Object Restrictions: Horizontal Agreements

Article 101 TFEU - Horizontal

- **There are 4 key cartel agreements that incur the highest penalties and should never be entered into:**
 - ✓ **Price Fixing** – when firms agree to sell items at a price higher than they normally would if they were competing against each other.
 - ✓ **Restricting Supply** – When firms restrict the quantity of goods/services supplied with the intention of raising prices.
 - ✓ **Market Sharing** – When firms agree to operate only within agreed areas in the country.
 - ✓ **Bid Rigging** - When businesses agree, when bidding for a contract, which one will win that contract and at what price.



Object Restrictions: **Horizontal Agreements**

Article 101 TFEU - Horizontal

▪ A word on Exchange of Information among Competitors:

- ✓ **Exchange of Information** – Exchanges of information are interactions among competitors that, from a competition law perspective, fall between hard-core “naked” cartels and cooperation, which leads to increased transparency in the market which can both bolster allocative and productive efficiencies.

For example, competing firms often exchange information in order to make more informed market decisions which can help to overcome market inefficiencies. However, case law has shown that information exchange may also enable firms to engage in collusion more readily and sustain it longer.

- The main competition law concern arises when the nature of the information exchanged between current or potential competitors makes it easier for them to predict each others' behaviour and adjust their own accordingly. This in its most severe form may ultimately enable participants to fix prices or allocate customers or markets, in other words to participate in a cartel.



Object Restrictions: Information Exchange

Article 101 TFEU - Horizontal

- Irrespective of whether a meeting is held in a formal or informal setting, or under the guise/guidance of a trade association, legal advice should be obtained before businesses share any current information relating to the following areas:
 - prices and pricing strategy including discounts, rebates, etc.;
 - methods by which prices are calculated;
 - terms and conditions of business, promotions and special offers;
 - general market strategy; or
 - other information which a competitor would not normally be able to discover.

The golden rule is that any exchange or disclosure of information should not enable you to reduce uncertainty, that is, in a way that enables you to forecast more precisely the competitive conduct of your competitors or reduce the degree of uncertainty about the operation of the market which would have existed in the absence of such an exchange of information.



Object Restrictions: Information Exchange

Article 101 TFEU – Horizontal – *Talking around prices can be just as bad as talking about them directly*

- **Example (Object) – Bananas (2015) In Case COMP/39188** –(upheld in Case C-286/13 P Dole Food and Dole Fresh Fruit Europe v Commission)
- The Commission fined Dole, Weichert and Chiquita for engaging in bilateral pre-pricing communications about price-setting factors for bananas. The parties discussed (ahead of the quotation price setting and announcement to customers) factors relevant to quotation prices each Thursday, for the forthcoming week. The quoted prices were not, however, the prices that were finally agreed by each supplier separately with their respective customers. These quotation prices served as signals to the market about the trends and/or indications as to the intended movement in prices of bananas for the following week.
- I.E. the exchange of information did not form part of a broader cartel + there is no direct link between the conduct and consumer prices
- The Commission found that this **reduced the uncertainty** between the parties as regards their price quotations.
- Second, after the prices were set, the parties exchanged their quotation prices bilaterally. The Commission found that **this enabled the companies to monitor individual pricing decisions** in light of pre-pricing communications.



- In their appeal the Dole companies claimed that the GC had made a mistake in law by finding that the pre-pricing communications constitute a restriction of competition by 'object'. That was an incorrect legal characterisation of the facts, because the IE cannot be regarded as *capable of removing uncertainty* as to their intended conduct regards the setting of actual prices.
- The ECJ disagreed:
 - It recalled its standard caselaw that for an agreement/concerted practice to be prohibited by Article 101 (1) TFEU, it must have 'as [its] object or effect' the prevention, restriction or distortion of competition in the internal market. Thus, certain types of coordination between undertakings reveal a 'sufficient degree of harm to competition' that it may be found that there is no need to examine their 'effects' (CB v Commission, C-67/13 P, EU:C:2014:2204, paras 49 - 50).
 - In order to determine whether a type of coordination between undertakings reveals a sufficient degree of harm to competition = a restriction of competition 'by object', regard must be had, inter alia, to its objectives and the economic and legal context of which it forms a part
 - The parties intention is not relevant although taken into consideration in this analysis
 - In particular, an exchange of information which is capable of removing uncertainty between participants as regards the timing, extent and details of the modifications to be adopted by the undertakings concerned in their conduct on the market must be regarded as pursuing an anticompetitive object (T-Mobile Netherlands and Others, C-8/08, EU:C:2009:343, para 41).
 - Moreover, a concerted practice may have an anticompetitive object even though there is no direct connection between that practice and consumer prices. Indeed, it is not possible on the basis of the wording of Article 101(1) TFEU to conclude that only concerted practices which have a direct effect on the prices paid by end users are prohibited (judgment in T-Mobile Netherlands and Others, C-8/08, EU:C:2009:343, paragraph 36).
 - On the contrary, Article 101(1)(a) TFEU provides that concerted practices may have an anticompetitive object if they 'directly or indirectly fix purchase or selling prices or any other trading conditions' (judgment in T-Mobile Netherlands and Others, C-8/08, EU:C:2009:343, para 37).



Object Restrictions: **Horizontal Agreements**

Article 101 TFEU - Horizontal

- **Example (Effect) – Asnef-Equifax Case C-238/05 of 23 November 2006**
- The CJEU was asked to review the compatibility with the European competition rules of an online register set up by the Spanish association of financial institutions as credit providers.
- The register contained sensitive information on existing and potential borrowers, such as past credit history, failures to pay, outstanding credit balances etc.
- The purpose of the register was to better inform lenders as to risks connected with granting loans, leading to greater and more efficient availability of credit. The point of the system was to allow the said providers to figure out the likelihood of repayment by potential borrowers
- The CJEU concluded that the information exchanged on the creditworthiness of potential borrowers served to reduce the risk of lending by reducing the disparity between the information available to credit institutions and that held by potential borrowers.
- Therefore, the information exchange was capable of reducing the number of borrowers who default on repayments, and hence improved the functioning of the credit supply system as a whole, leading to a more efficient market outcome.
- As the credit register was **designed to limit risks of credit institutions** in granting loans, the Court concluded that the exchange of information **did not have the object** of restricting competition.

RECAP: IE Framework for Assessment

- To be caught by Article 101 TFEU, the IE must have as its object or effect the prevention, restriction or distortion of competition within the internal market:
- Restriction of competition by **object**: IE will be considered a restriction of competition by object where the information is commercially sensitive and the exchange is capable of removing uncertainty between participants as regards the timing, extent and details of the modifications to be adopted by the undertakings concerned in their conduct on the market.
- Restrictive **effects** on competition: it must be likely to have an appreciable adverse effect on one or more aspects of competition, such as price or product variety or innovation. Whether an IE will have restrictive effects will depend on the nature of the information exchanged, the economic conditions of the relevant market(s) and the characteristics of the information exchange.
- The key test for object or effect: whether the flow of information reduces the **strategic uncertainty** of competitors, consequently diminishing their incentives to compete one against the other.
- **Information is commercially-sensitive**: if related not only to prices (for example, actual prices, discounts, increases, reductions or rebates), but also costs, capacity, production, quantities, market shares, customers, plans to enter or exit markets, or other important elements of a firm's strategy that undertakings active in a genuinely competitive market would not have an incentive to reveal to each other.



RECAP: IE Framework for Assessment

- If an information exchange meets the criteria under Article 101(3), it will not be prohibited under Article 101(1). An assessment under Article 101(3) will examine
 - Whether the information exchange leads to significant efficiency gains.
 - Type of Info: type of data, amount of information, aggregation, age, confidentiality and frequency of the exchange are indispensable for creating the efficiency gains. Restrictions that go beyond what is necessary to achieve efficiency gains do not fulfil the requirements of Article 101(3).
 - Efficiency Gains: obtained by the indispensable restrictions are passed on to consumers to an extent that outweighs the restrictive effects on competition caused by an information exchange. The lower the market power of the companies exchanging information, the more likely it is that efficiency gains passed on to consumers outweigh the restrictive effects on competition.
 - Competition is eliminated: or could potentially be eliminated in respect of a substantial part of the products concerned as a result of the information exchange (in which case, the conditions of Article 101(3) will not be met).
- Unlike for other types of horizontal co-operation agreements, the 2023 Horizontal Co-operation Guidelines do not set out any safe harbour.
- They provide guidance on the relevance of the nature of the information exchanged for the assessment under Article 101(1) of the TFEU, the characteristics of the exchange and the characteristics of the market. They also provide guidance on information exchanges that restrict competition by object and by effect and on the application of Article 101(3).



Object or Effect: **Vertical Agreements**

Article 101 TFEU - Vertical

➤ The categories of vertical agreements that are typically treated by the Commission as having the **object** of restricting competition are those that are deemed to be "hardcore" agreements for the purposes of the vertical agreements block exemption for example:

- Imposition of fixed or minimum resale prices.
- Restrictions of passive sales (including sales over the internet) in exclusive distribution agreements.
- Restrictions of cross-supplies between members of a selective distribution arrangement.
- Restrictions of cross border sales



Object or Effect: **Vertical Agreements**

Article 101 TFEU - Vertical

▪ **Example – Supplier and Distributor Arrangement**

White Clauses

- (i) technical information relating to the products or services,
- (ii) logistical information, including information on production processes, inventory or stocks,
- (iii) customer information, for ex in terms of preferences or feedback on the products,
- (iv) but also information on resale prices, provided however that such information is not used by the supplier to engage in resale price maintenance.

Grey clauses

- (i) Information relating to the actual future prices at which the supplier or buyer would sell the contract goods or services downstream
- (ii) Customer-specific sales data, including non-aggregated information on the value and volume of sales per customer, or information that identifies particular customers (unless necessary to enable the adaption of contract goods/services to the consumers' requirements or to provide guarantee or after-sales services, or to allocate customers under an exclusive distribution agreement).



Article 101 - Moving on to Vertical Agreements



Sample Distribution Agreement

DRAFT FOR DISCUSSION PURPOSES ONLY

DISTRIBUTION AGREEMENT

Between

[_____]

and

[_____]

Draft 1 - for discussion purposes only



Methodology for Assessment for Verticals



An Article 101 Analysis of a Vertical Agreement

Diploma in Law (Malta)



Meliá Hotels International, S.A. ('Meliá') – Summary of Facts

Meliá, is one of the largest hotel companies in the world and the largest hotel chain in Spain in both resort and city hotels.

The case concerned agreements regarding hotel accommodation concluded between Meliá and certain tour operators (Kuoni, REWE, Thomas Cook and TUI), which sourced accommodation from Meliá and distributed it to consumers.

From 1 January 2014 to 31 December 2015, approximately 30% of the contracts governing the commercial relationship between Meliá and the tour operators contained a clause according to which the contracts were valid only for reservations of consumers who were resident in specified countries.

If Meliá established that the country of residence of the consumer was not among those listed in the contract, Meliá was entitled to reject the reservation.



An Article 101 Analysis of a Vertical Agreement

Diploma in Law (Malta)



Meliá Hotels International, S.A. ('Meliá') – Legal analysis

Article 101(1) TFEU = involving the implementation and enforcement of a series of agreements aimed at restricting active and passive cross-border sales hotel accommodation which has as its 'object' the restriction of competition within the meaning of Article 101(1) TFEU.

The Commission concluded that Meliá's practices restricted the ability of the tour operators to sell freely the hotel accommodation in all EEA countries and to respond to direct requests from consumers who were residents outside the defined countries. As a result, consumers were not able to see the full hotel availability or book hotel rooms at the best prices with tour operators in other Member States.

The Commission emphasized that the cross-border sales restrictions in the contracts were liable to affect trade between Member States, since this was the very purpose of the contracts. Therefore, the contracts = appreciable effect on trade between Member States.



An Article 101 Analysis of a Vertical Agreement



Meliá Hotels International, S.A. ('Meliá') – Article 101(3) TFEU
– no block or individual exemption

The Commission confirmed that, due to the hardcore nature of the restrictions, the Vertical Block Exemption Regulation or 'VBER' at that time did not apply.

Despite the presence of a hardcore restriction in an agreement, the conduct could however possibly still be exempted under Article 101(3) TFEU. In this case, however, the Commission decided that the conditions for such an individual exemption were not fulfilled. The main reasons were that:

- Meliá did not provide any arguments in this respect;
- consumers would not get a fair share of the resulting benefit; and
- clauses that restrict the ability of tour operators to sell accommodation to consumers outside of specified country/countries were not indispensable for improving the efficiency of Meliá hotel accommodation.



Article 101 - Vertical Agreements

- "Vertical agreements" are defined as agreements entered into between two or more undertakings each of which operates, for the purposes of the agreement, at a different level of the production or distribution chain, and which relate to the conditions under which the parties may purchase, sell or resell certain goods or services

- "Vertical restraints" are restrictions of competition contained in vertical agreements (Article 1(1)(b)).

- There are three elements to this definition:
 - i. The agreement must be between two or more undertakings.
 - ii. Each undertaking must operate, for the purposes of the agreement, at a different level of the production or distribution chain.
 - iii. The agreement must relate to the conditions of purchase, sale or resale of services or goods. This means that vertical agreements relating to goods and services, final and intermediate, are all covered.



Vertical Restraint**Definition****Single Branding**

Buyer is obliged/forced/induced/incentivised to purchase all or most of its requirements from only one supplier, that is, not to buy and resell competing goods/services.

Exclusive Distribution

Where the supplier agrees to sell its products only to one distributor for resale in a particular territory (and where usually the distributor is restricted from active selling into other exclusively allocated territories)

Exclusive Customer Allocation

Where the supplier limits sales to only one buyer for a certain class of customer

Selective Distribution

Where the supplier agrees to sell the contract goods/services, directly or indirectly, only to dealers selected on the basis of certain pre-defined qualitative or quantitative criteria and where those dealers agree not to sell to unauthorised dealers

Exclusive Supply

Where the supplier agrees, or is incentivised, to sell only or mainly to one buyer

Resale Restrictions

Buyer is obliged/induced not to resell the contract goods below certain price levels: minimum resale prices, fixed resale prices, recommended or maximum resale prices



Article 101 – Introducing the VBER

- The Vertical Block Exemption Regulation (VBER) creates an exception to the principles of the cartel prohibition for certain vertical agreements.
- The European Commission has adopted the new Vertical Block Exemption Regulation ('VBER') accompanied by the new Vertical Guidelines, following a thorough evaluation and review of the 2010 rules.
- The current revision is mainly due to the growing digitalisation of the economy, the unstoppable growth of online sales along with the expansion of large e-commerce companies and platforms.
- The European Commission had also already noticed that certain matters wrongly fell outside or within the block exemption, so that in certain cases the rules appeared to be either too strict or not strict enough.
- The revised rules provide businesses with simpler, clearer and up-to-date rules and guidance. The new rules will help them to assess the compatibility of their supply and distribution agreements with EU competition rules in a business environment reshaped by the growth of e-commerce and online sales.
- The revised VBER (Commission Regulation (EU) 2022/720) and Vertical Guidelines came into force on 1 June 2022.



Article 101 – Introducing the VBER

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The VBER: Regulation 2022/720

The Presumption under the VBER

- Where the market share held by each of the parties in a Distribution Agreement falls below **30%** and
- there are no **severe restrictions** on competition e.g., RPM
- it is presumed that the agreement will lead to an improvement in the market, with consumers ultimately benefiting from the arrangement.

Above 30%

- If the market share exceeds the 30% threshold, there is no presumption of illegality, but companies are encouraged to make their own assessment of an agreement in order to determine whether it restricts competition



Hardcore Restrictions

- The VBER contains a "blacklist" of vertical restraints which, if included in a vertical agreement, will mean that the block exemption cannot apply (despite the fact that the market share threshold is not exceeded) (Article 4).
- The inclusion of any such restraint prevents the entire agreement from obtaining the benefit of the VBER, not merely the clause or sub-clause in which the restraint is contained: there is no severability for hardcore restrictions for the purposes of the block exemption.
- Exemption of hardcore restraints is unlikely, but undertakings can demonstrate pro-competitive effects under Article 101(3) in any individual case.
- OVERVIEW of the hardcore restrictions or blacklisted restrictions under VBER :
 - i. Resale Price Maintenance
 - ii. Territorial or Customer Restrictions
 - iii. Sales by a Selective Distribution System
 - iv. Online Restrictions



Hard Core (1) – Resale Price Maintenance

Resale Price Maintenance	
RPM constitutes the first of the hardcore restrictions described in Article 4(a) VBER. RPM, as a hardcore restriction, is presumed (i) to fall within the scope of Article 101(1) TFEU (definition of anticompetitive agreement) and (ii) not to satisfy the conditions of Article 101(3) TFEU (efficiency defence).	<ul style="list-style-type: none"> • Minimum or fixed prices are not permitted • Recommended provided they do not amount to a fixed or minimum amount as a result of incentives or threats by the supplier • Maximum prices are permitted
The European Commission recognizes that in some circumstances, RPM may be necessary to achieve certain efficiencies, in which case the agreement will be exempted under Article 101(3) TFEU.	<ul style="list-style-type: none"> • the launch of a new product • short-term promotion and • additional pre-sales services provided by retailers.
Example: A clause that makes the grant of rebates conditional to adherence to the general price level is invalid	



What amounts to RPM?

- Fixing the distributor's margin;
- setting a maximum discount which a distributor must apply;
- Minimum advertised prices

[policies which prohibit retailers from advertising prices below a certain level set by the supplier. For example, such policies may infringe competition law if the supplier sanctions distributors for ultimately selling below the set level or prevents them from communicating that the final price could differ]

- making rebates or promotional costs (or other supply benefits) conditional upon adherence to a given price level;
- linking the resale price to that of competitors' products;
- using threats, intimidation or warnings to coerce a buyer to comply compliance with the supplier's recommended resale prices;
- indirect pressure linked to mechanisms to identify instances of discounting;
- monitoring the prices of distributors; and
- obliging retailers to report other distributors deviating from the "recommended" price level.



ASUS & Co and RPM



The Commission found Asus, Denon & Marantz, Philips and Pioneer to have engaged in so-called **fixed or minimum resale** RPM by restricting the ability of their online retailers to set their own retail prices for widely used consumer electronics products — such as kitchen appliances, notebooks, and hi-fi products.

- The manufacturers put pressure on ecommerce outlets who offered their products at low prices, writing, *“If those retailers did not follow the prices requested by manufacturers, they faced threats or sanctions such as blocking of supplies.”*
- The Commission specifically pointed to the fact that the companies had used sophisticated algorithms to monitor the prices set by distributors, thereby allowing them to intervene quickly when there were price decreases.
- Asus in particular had monitored retailers' resale prices for certain computer hardware and electronics products and had intervened with retailers in two EU Member States (Germany and France) that were **selling their products below Asus's recommended resale prices**, and had asked them to increase their prices.
- The Commission concluded that this practice had had the effect of limiting effective price competition, thus leading to higher prices for consumers.



Hard Core (2) Territorial or Customer Restrictions

First Things First: An Important Definition of Sales

Active sales involve some form of active targeting of a particular customer group or territory.

Passive sales consist of transactions in response to unsolicited requests from individual customers without having initiated the sales by means of active targeting of such customers.

Ex., So, if a distributor sends mail to a particular customer, there is an active sale when, that customer places an order. On the contrary, if the customer has picked up some general advertising in a magazine and visits the shop of the distributor, the subsequent sale is a passive sale.

There are numerous variations on the same theme, but the dividing line in legal terms is clear. It depends on the party that took a targeted initiative to arrive at the transaction. In the case of active selling, it is the distributor who does so. With passive sales, the initiative rests with the customer.



Active sales

- Actively approaching individual customers
- Sending direct mail
- Sending unsolicited e-mails
- Sales visits
- Actively approaching a specific customer in a specific territory through advertisement in media, on the internet or other promotions specifically targeted at that customer in that territory
- Online advertisement specifically addressed to certain customers
- Territory-based banners on third party websites
- Paying a search engine or online advertisement provider to have advertisements displayed specifically to users in a particular territory



Passive Sales

- Responding to unsolicited requests from individual customers
- General advertising or promotion that reaches customers in other distributors' (exclusive) territories or customer groups, but which is a reasonable way to reach customers outside those territories (including customers in one's own territory)
- Using a website to sell products (in general, that is, unless it is specifically targeted at particular customers)
- A customer visiting the website of a distributor and contacting the distributor, leading to a sale, including delivery
- A customer visiting the website of a distributor and opting to be kept (automatically) informed by the distributor, leading to a sale. (Even if a distributor's website offers different language options, this does not change the passive character of such selling)



Hard Core (2) – Territorial or Customer Restrictions

Territory or Customer Restrictions – Exclusive Distribution

In order to protect efforts and investments made by exclusive, but non-selective distributors, the VBER accepts under strict conditions that other distributors may be obliged to refrain from active selling into the territory or to a customer group that is allocated to an exclusive distributor(s).

The VBER enables suppliers to:

- (i) appoint up to 5 distributors per exclusive territory or customer group
- (ii) restrict active or passive sales to unauthorised distributors located in a territory where there is a selective distribution system

- Restriction on active sales only permitted in relation to exclusively allocated territories or customers
- No Restriction permitted on passive sales
- Parallel Imposition: the supplier must impose the active sales restriction on all its other buyers.
- Roll over: the supplier can oblige its exclusive distributors to pass their active sales ban on to their direct customers

Example: Non-exclusive distributors A and B in territory X might be prevented from actively selling into territory Y that has been exclusively allocated to distributor C. But, un-intuitively, C cannot be prevented from actively selling in X (despite its exclusive status in Y) because X is a non-exclusive territory.



Types of Territorial Restrictions

Direct obligations

- Obligation not to sell or supply certain customers or territories
- Obligation to refer orders from those customers to other distributors
- Export bans

Indirect measures aimed at inducing compliance/monitoring

- Refusal or reduction of bonuses or discounts
- Termination of supply
- Price discrimination – higher price for exported products
- Failure to provide EU-wide guarantee service



Quick Ex of Restrictions on Out of Territory Sales



“Football fans often cherish branded products from their favourite teams, such as jerseys or scarves. Nike prevented many of its licensees from selling these branded products in a different country, leading to less choice and higher prices for consumers. This is illegal under EU antitrust rules”

Margrethe Vestager, EU Commissioner

Nike's core business is the design and sale of athletic footwear and apparel, including for football clubs and federations, which generally feature Nike's registered trademarks, such as its name or “Swoosh” logo. Other products, so-called “licensed merchandise”, only feature the brands of a football club or a federation, not Nike's trademarks. For these products, Nike acts as a licensor of IPRs that grants licences to third parties, who become entitled to manufacture and distribute those products. It is in the context of Nike's role as a licensor for the manufacture and distribution of these licensed merchandise products that the Commission is imposing a fine.



Quick Ex of Restrictions on Out of Territory Sales

In its decision the Commission found a series of “practices” restricting active and passive cross-border sales of the licensed products.

Namely,

- a) **direct measures** (contract clauses) restricting out-of-territory sales by licensees, such as (i) prohibitions of out-of-territory passive (including online) and active sales; (ii) obligations to refer orders for out-of-territory sales or queries to Nike; and (iii) clauses clawing back royalties and revenues deriving from out-of-territory sales;
- b) **indirect measures** restricting out-of-territory sales by licensees such as threats to end the agreements selling outside their allocated territories;
- c) restrictive practices implemented vis-à-vis master licensees to compel them not to sell outside their territories and to **enforce restrictions vis-à-vis their sub-licensees** on behalf of Nike; and
- d) Prohibited **out-of-territory online sales** – from 2012, Nike began to restrict licensed merchandise from being marketed on websites that were accessible outside of the relevant licensee's allocated territory.



An example of a French supplier and a Dutch distributor

The assignment of territory protection in a distribution agreement is not deemed to be a 'hardcore' restriction provided that 4 conditions are met. In that case a benefit can be obtained from the VBER. The cumulative conditions are:

1. Both the supplier and the distributor may not have a **market share** that exceeds 30%;
2. A geographic territory or block of customers must be **assigned exclusively** to a distributor(s);
3. **Active selling** may be prohibited, **passive selling** must be permitted;
4. The distributor must be protected against active selling by others (**parallel imposition**)



- i. a French supplier that distributes its products directly in France but that wishes to distribute its products in the rest of the EU via distributors, and
 - ii. a Dutch distributor that is assigned the Netherlands as an exclusive territory by the French supplier
- You have a vertical agreement between supplier and distributor;
 - So the VBER may apply depending on market share;
 - The VBER may apply provided there are no Hard Core Restrictions;
 - In this case one would have to assess the restriction by territory



I. The 1st condition for the VBER to apply: market threshold of 30% for supplier and distributor

➤ Firstly, the application of the block exemption requires that both the supplier and the distributor do not have a market share that exceeds 30%. If those market shares are exceeded, it will not be possible to benefit from the block exemption.

I. The 2nd Condition: Exclusive Assignment

➤ This means that the French supplier assigns the territory of the Netherlands exclusively to the (in this case Dutch) distributor (but up to five distributors)



III. The 3rd condition: active selling ✓ but passive selling ✗

- The French supplier must impose a prohibition on its other buyers other than the Dutch distributor with regard to preventing them from actively selling to customers in the Netherlands.
- E.g., If German distributor sells products via a website it is also prohibited from, for e.g., paying search engines to display its website when searches are made from the Netherlands (these are targeted forms of advertising)
- But the exclusive Dutch distributor will have to accept the passive selling by other distributors in its territory or to its block of customers, since the French supplier is only able to restrict the active selling



IV. The 4th Condition: Parallel Imposition –

- This means that if the French supplier fails to prohibit active selling in the Netherlands by its other (European) distributors, the Dutch distributor is not protected against active selling in the Netherlands and the other distributors can simply acquire customers in the Netherlands. In effect and from a legal perspective, the Dutch distributor therefore has no exclusive territory, while this is what was agreed between the French supplier and the Dutch distributor
- In this example therefore, on the one hand, when for instance the French supplier prohibits the active selling in the Netherlands by German distributors, while that ban is not imposed on distributors from other MS, the competition between the German and all other distributors is restricted. German distributors are the only party specifically refused access to the Dutch market
- The French supplier will therefore do well to ensure that all agreements with distributors contain a parallel imposition or a prohibition on active selling in the Netherlands. If not, it runs the risk of being faced with a claim for compensation from the Dutch distributor, because the French supplier has not fulfilled what it should have done on the basis of the block exemption and the agreement: protect the Dutch distributor.



Hard Core (3) Selective Distribution System

First things First – what is a SDS?

- **Why?** An SDS will typically be used by a supplier to achieve a consistent standard and quality of service in the outlets where the products are sold
- **What is an SDS?** In such a system, the supplier agrees to supply only those distributors who meet certain minimum (qualitative or quantitative) criteria. The distributors, in return, agree to supply only other “selected” or authorised distributors who are within the approved SDS OR end users
- **What products are eligible?** These systems are often used for the distribution of complex/technical consumer products or luxury/branded goods where there is a brand image to protect or where there is a need to preserve quality or to explain its use.



The Selection Criteria for an SDS

Examples of permitted qualitative criteria:

- Suitably trained staff
- To sell the products in a specialised shop or display
- Providing an after-sales service which is compliant with the product warranty

Examples of quantitative criteria which would be permitted:

- Buying a minimum quantity of goods
- Achieving a particular turnover
- Maintaining minimum stock



Hard Core (3) Resale by members of a SDS

Resale in a Selective Distribution System (SDS)

In a SDS the supplier undertakes to sell the contract products, either directly or indirectly, only to distributors who satisfy certain objective criteria. Selective distributors are free however to sell to all end-users without limitation.

The Supplier cannot:

- i. restrict cross-supplies between the members of the SDS operating at the same or different levels of trade

The dealers in a selective distribution system cannot therefore be restricted as to the users to whom they sell, including via internet sales

Restriction on active and passive sales to unauthorised distributors

Restriction of active sales by members of the SDS, into a territory or to a customer group allocated by the supplier exclusively to a maximum of five exclusive distributors



Guess and its SDS



- Guess, a US-based company active in the clothing, shoes and accessories sector, employed a selective distribution system at the wholesale and retail level of trade. It also sold its products online directly through its own online shop and as a seller on online marketplaces.
- Guess Europe sold the contract products only to distributors selected on the basis of specified selection criteria and, second, the selected distributors are prohibited from selling the contract products to other distributors not belonging to the selective distribution network = Guess Europe's distribution network fulfilled the criteria to qualify as a selective distribution system
- The Commission fined the US Guess EUR 39.8 million for anti-competitive practices in its European selective distribution system. Guess had imposed various restrictions:

restrictions on cross-border sales and online advertising, which enabled the company to maintain artificially high retail prices, particularly in Central and Eastern Europe; and **Cross network sales which** must not be restricted either among authorised wholesalers, or among authorised retailers and wholesalers



A bit more on this case and Article 101 TFEU

- **Online search advertising restrictions:** Guess banned retailers from using or bidding on Guess brand names and trademarks as keywords in Google AdWords.

In so doing, Guess sought to maximize traffic to its own website and minimize its own advertisement costs. This restricted the 'findability' and ultimately the viability of the online retailers in Guess' selective distribution system;

- **Online sales restrictions:** Authorized retailers were contractually obliged to first obtain explicit authorization from Guess to conduct online sales. In addition, Guess did not specify quality criteria for online sales and had full discretion in deciding whether retailers were allowed to sell online.

The primary objective was to protect Guess' own online sales activities and to limit intra-brand competition by authorized retailers;

- **Restrictions on cross-selling:** Guess prevented wholesalers and retailers from cross-selling to each other by imposing outright sales restrictions and applying disincentives to cross-sales. This was done through different types of clauses in the respective wholesale and retail agreements, for example:
 - a restriction on wholesalers to promote or advertise outside their allocated territory, in some cases subject to termination of the agreement;
 - restrictions on retailers on purchases across the selective distribution network, only allowing sales to end users
- **Restrictions on cross-border sales to end users:** Guess imposed restrictions on active and passive sales by retailers to end users located outside their allocated territory.



A bit more on this case and Article 101 TFEU cont.

- **Online search advertising restrictions:** Guess claimed that the restriction served the legitimate objective of protecting Guess' brand image. The Commission refuted this claim and concluded that the restriction had as its object to reduce the ability of authorized retailers to advertise and ultimately to sell the contract products to customers, in particular outside the contractual territory or area of activity, and to limit intra-brand competition.
- **Online sales restrictions:** The Commission found that Guess sought to protect its online sales activities from intra-brand competition and to limit the retailers' ability to sell outside their territory and concluded that this conduct constitutes a restriction of competition by object within the meaning of Article 101(1) TFEU.
- **Restrictions on cross-selling:** The Commission reiterated settled case law that a restriction of sales between authorized distributors constitutes a restriction of competition by object within the meaning of Article 101(1) TFEU, and concluded that the restrictions on cross-selling imposed by Guess restricted competition by object.
- **Restrictions on cross-border sales to end users:** The Commission found that these restrictions were capable of creating, maintaining or restoring national divisions in trade between Member States and therefore it concluded, in accordance with settled case law, that they restricted competition by object within the meaning of Article 101(1) TFEU.



Hard Core (4) Online Sales

Online Sales

The prevention of the effective use of the internet by the buyer or its customers to sell the contract goods or services, as it restricts the territory into which or the customers to whom the contract goods or services may be sold is prohibited

The Supplier can impose:

- i. other restrictions of online sales; or
- i. restrictions of online advertising that do not have the object of preventing the use of an entire online advertising channel

- **ban sales on online marketplaces, provided that they do not constitute a hardcore restriction and prevent the effective use of the internet by the distributors and their customers**
- **Clarification of restrictions such as prohibiting online advertisement including the use of price comparison tools and online search engines**



Case C-439/09 Pierre Fabre – Ban on Online Sales



- PF is a French-based company that manufactures and markets cosmetic and personal care products under brands such as Avène, mainly through pharmacies, in France and the EU. The general conditions of distribution and sale of these products required that the sales “*be made exclusively in a physical space, in which a qualified pharmacist must be present*”, thus excluding de facto any form of online sales.
- French NCA concluded that this ban imposed on its authorized distributors amounted to a restriction on competition contrary to Article 101 TFEU and corresponding French law. PF challenged the decision before the Paris CoA, claiming that it unlawfully denied the contested practice the (i) benefit of the VBER and that of (ii) an individual exemption.
- The CoA referred a preliminary question to ECJ on whether a general and absolute ban on selling contract goods to end-users via the internet, imposed on authorized distributors in the context of a selective distribution network, constitutes a hardcore restriction of competition for the purposes of Article 101(1) TFEU, which is not covered by the block exemption, but which is potentially eligible for an individual exemption under Article 101(3) TFEU.



Case C-439/09 Pierre Fabre – Ban on Online Sales



Legal analysis- Article 101(1) TFEU – applicability

- The ECJ stated that agreements constituting a selective distribution system are to be considered as restrictions by object in the absence of objective justification. In fact, a (purely qualitative) distribution system is objectively justified, and therefore outside the scope of Article 101(1) TFEU, to the extent that the Metro criteria (Case 26/76 Metro SB-Großmärkte) are fulfilled, which is the case if:
 - i. the resellers are chosen on the basis of objective criteria of a qualitative nature;
 - ii. the criteria are laid down uniformly for all potential resellers and not applied in a discriminatory fashion;
 - iii. the characteristics of the product in question necessitate such a network in order to preserve its quality and ensure its proper use; and
 - iv. the criteria do not go beyond what is necessary.



Case C-439/09 Pierre Fabre – Ban on Online Sales



Legal analysis- Article 101(1) TFEU – applicability

- The ECJ noted that it had not accepted arguments relating to the need to provide individual advice to the customer and to ensure his protection against the incorrect use of products, in the context of non-prescription medicines and contact lenses, to justify a ban on internet sales; and
- It also noted that the aim of maintaining a prestigious image is not a legitimate aim for restricting competition and cannot therefore justify a finding that a contractual clause pursuing such an aim does not fall within Article 101(1) TFEU.



Case C-439/09 Pierre Fabre – Ban on Online Sales



Article 101(3) TFEU – no block exemption

- An online sales ban has as its object the restriction of passive sales to end users wishing to purchase online and located outside the physical trading area of the relevant member of the selective distribution system. The ban on internet sales in the context of a SDS cannot benefit from the VBER because such a ban operates as a limitation on active and passive sales pursuant to Article 4(c) of the (old) VBER.

Article 101(3) TFEU – possibility of an individual exemption

- a contract may benefit, on an individual basis, from the exception of Article 101(3) TFEU where the conditions of that provision are met. The ECJ however did not have sufficient information to assess this. As said, the referring court found that the conditions for the application of Article 101(3) TFEU were not met, a.o. because an online sales ban was not indispensable to achieve the aim of Pierre Fabre.
- It also noted that the aim of maintaining a prestigious image is not a legitimate aim for restricting competition and cannot therefore justify a finding that a contractual clause pursuing such an aim does not fall within Article 101(1) TFEU.

Case C-230/16 EU:C:2017:941

You have been requested to advise a client – Coty Germany GmbH (“Coty”), a supplier of cosmetic luxury products which operates a SD system;

It has a dispute with one of its authorized retailers in Germany Akzente

Akzente may:

- Sell via its own internet platform
- Sub-contract internet platform design to 3rd party
- But It cannot sell via Amazon.de

Can client impose a 3rd PARTY PLATFORM BAN?
Does client have any objective justifications?



Application of the OLD VBER

The case comes as a result of a request by the Higher Regional Court of Frankfurt, to the ECJ, for a preliminary ruling regarding the interpretation of Article 101(1) TFEU and Article 4(b) and (c) of Commission Regulation (EU) No 330/2010 (OLD VBER)

➤ **One of the key questions to be answered was:**

Whether a prohibition on engaging third-party undertakings, discernible to the public, to handle internet sales, imposed on members of a selective distribution system, was a hardcore restriction under either Article 4(b) or Article 4(c) of the VBER



Application of the OLD VBER

- Coty's and Akzente's market shares were below 30% (Art. 3)
- **QUESTION: Was the ban on 3rd party platforms black-listed? (Article. 4)**
- **4(b): the restriction of the territory into which, or of the customers to whom, a buyer party to the agreement may sell the contract goods or services**

There is no such thing under VBER as a category of 3rd party platform purchasers

- **4(c): the restriction of active or passive sales to end users by members of a selective distribution system operating at the retail level of trade**

Akzente may advertise on its website on other websites or on search engines



Some Points to Consider before the Question Posed

- The reason why manufacturers of luxury products rely upon a SDS is not a secret. When products are sold through independent retailers, their reputation may suffer. There is also a risk that end-users' experience is not the same in all stores.
- The point of SDS is to ensure that only retailers that satisfy certain criteria are entitled to sell a given product; by imposing a set of a criteria to be satisfied by retailers, a manufacturer of luxury products can preserve the reputation of its products and a uniform end-user experience without resorting to vertical integration (which can be costly and thus limit its ability to expand or even enter the market).
- Therefore, by definition, this method of distribution only works if the retailers that are members of the system are prevented from selling to third parties that are not.
- Accordingly, a clause prohibiting resales to non-members is a textbook example of a restraint that falls outside the scope of Article 101(1) TFEU altogether
- Against this background, one key issue in Coty is whether prohibiting retailers from selling via online marketplaces = to a clause prohibiting sales to third-party retailers. It is not unreasonable to argue, in this sense, that the objective purpose of the two clauses is the same.



The CJEU on the Question Posed

- A marketplace ban neither (i) restricts the customers to whom authorized distributors can sell (ii) nor restricts passive sales to end users.
- A marketplace ban differs from an outright prohibition of the use of internet sales
- third-party platform customers are not a definable customer group in terms of Article 4(b), so that the ban did not exclude sales to a certain category of customers as a whole, which would have been illegal.
- Nor does it exclude (passive) online sales entirely, in terms of Article 4(c) given that distributors could still sell through their own web shops or non-discernible third-party platforms (e.g. price comparison websites) customers were usually able to find the online offer of authorized distributors.
- **Conclusion: marketplace bans are not hard core under VBER**



Outside the VBER

- If the vertical agreement does not conform to the criteria set out in the VBER, it will not benefit from the block exemption, **but it does not necessarily follow that the agreement is automatically void or unenforceable**
- In this situation, the parties must first legally assess whether the agreement is likely **to breach Article 101(1)**. If an analysis determines, on balance, that the agreement does not breach the prohibition, then the parties do not need to consider the matter any further
- If the agreement does fall within the prohibition however, the parties must go on to evaluate whether the benefits of the agreement justify imposing such restrictions on competition and whether the agreement satisfies the criteria for individual exemption as **set in Article 101(3)**



RECAP Quiz

Q1. May a supplier control the prices at which its distributor resells its products?

Q2. May a supplier influence resale prices in other ways, such as suggesting a minimum advertised price policy?

Q3. May a supplier restrict the geographic areas or categories of customers to which its distribution partner resells?

Q4. Is there a distinction between active sales efforts and passive sales that are not actively solicited, and how are those terms defined?

Q5. May a supplier restrict or prohibit e-commerce sales by its distribution partners?



Hypothetical Case: AirCo Ltd

- AirCo produces basic screws for use in aircraft, which it sells in the US and has a global share of approximately 18%
- AirCo wishes to begin distributing in the EU, beginning with France and Germany only (and with the rest of EU reserved to itself)
- Its distributors will accept significant financial risk
- AirCo has the following initial objectives:
 - appoint one exclusive distributor in each of France and Germany. AirCo wishes to prohibit these distributors from making sales into another territory;
 - Its chosen distributors each have about 20% shares in their respective markets
 - Reserve “global” customers to itself (regardless of order origin)
 - Prohibit its distributors from using the Internet under any circumstances



Analysis of AirCo Strategy

- Article 101 applies: The agreement is between separate firms
- Possible exemptions/exclusions: Agency unavailable distributor accepts risk
- De minimis unavailable (market shares exceeded)
- VBER – possible, assessment of market shares and specific restrictions required
- Unavailable if “hardcore” restrictions or if market shares exceeded
- Only limited availability if “excluded” restrictions are present
- If VBER unavailable, a full assessment under Article 101(3) is necessary



Application of the VBER

Market Share

- Market shares within VBER limits ($\leq 30\%$) AirCo has a global share of 18%
- AirCo's distributors each have approximately 20% share

Assessment of specific restrictions required

- Territorial restrictions as each distributor is only permitted to sell in its allocated territory
- Customer restrictions - AirCo reserves "global" customers to itself
- Channel restrictions - Distributors are not permitted to use the Internet under any circumstances



Application: Territorial Restrictions

- **Territorial restrictions under EU competition law - AirCo's territorial restriction is potentially "hardcore" and would make the VBER unavailable and likely cause the agreement to infringe Art. 101**
- Why is AirCo's restriction potentially "hardcore"? A supplier may prohibit a distributor from "actively" seeking sales outside its territory
- BUT a supplier may not prohibit a distributor from filling unsolicited ("passive") orders requested by customers outside its territory
- Potential fix to enable AirCo to confer maximum exclusivity, while still applying the VBER (or reducing risk of infringing Article 101) AirCo can prohibit its distributors in France and Germany from making "active" sales outside of France and Germany, but not from filling unsolicited orders (including over the Internet)



Application: Customer Restriction

- **Customer restrictions - This restriction is potentially hardcore. A supplier is permitted to reserve a customer group to itself (or to another distributor) consistent with the VBER and, more broadly, EU competition law**
- Why is AirCo's customer restriction potentially hardcore? Because it threatens a distributor's ability to fill passive orders, which creates risks to the single market
- BUT a supplier cannot prohibit a distributor from filling unsolicited (passive) orders sought by customers in that group
- Potential fix to enable AirCo to reserve global customers, while still applying the VBER (or reducing risk of infringing Article 101) - AirCo can reserve to itself global customers, but it cannot prohibit its distributors in the EU from filling unsolicited orders from these customers



Application: Channel Restriction

- **Channel restrictions under EU competition law - This restriction is hardcore**
- Why is AirCo's Internet restriction hardcore? - The Internet must be available to all distributors, consistent with the VBER and a total restriction on use of the Internet is unlikely to be compliant with EU competition law
- There is no fix for this restriction, but AirCo can create guidelines for Internet use. If AirCo wishes to benefit from the VBER (and avoid infringing Article 101) it must not prohibit its distributors from using the Internet
- AirCo can impose reasonable guidelines on how its distributors use the Internet



AirCo Conclusions

- To ensure that the VBER is available, AirCo should amend its restrictions as follows:
 - Territories: AirCo can appoint an exclusive distributor for France and one for Germany. In this context, “exclusive” means that each distributor can be prohibited from making active sales outside of its territory, but not from filling passive (unsolicited) orders
 - Customers: AirCo can reserve global customers to itself, but it cannot prohibit its distributors from filling passive (unsolicited) orders received from these customers
 - Channel: AirCo cannot prohibit its distributors from using the Internet to sell its products, but it can introduce reasonable quality standards





Diploma in Law (Malta)



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