

Antitrust Law Blog

Posted at 1:36 PM on September 3, 2009 by Sheppard Mullin

EC Launches Consultation on Distribution Rules

I. Summary

On July 28, 2009, the European Commission (EC) launched a formal consultation on the EU rules applicable to distribution agreements. The current key legislation expires on May 31, 2010, and the intention appears to be to adopt the new rules before the end of this year. These proposals are important to both suppliers and retailers and affect both physical and online distribution. While the EC believes the current economic effects-based rules introduced in 1999 work well and do not need substantial change, it has published a revised draft Regulation and Guidelines that contain some important changes and clarifications from the existing law, in particular, with respect to internet sales, resale price maintenance, and purchasing power of large retailers.

II. Internet Sales

The EC seeks to strike a balance between allowing European consumers to take advantage of cross-border purchasing and protecting distributors who invest in marketing and promotion from other distributors who may "free-ride" on those efforts. The EC's draft Guidelines include significant new guidance in this area.

In particular, the EC makes a distinction between "active" sales in which a distributor actively approaches individual customers and "passive" sales in which a distributor responds to unsolicited requests from customers. If territories or customer groups are exclusively allocated to different distributors, restrictions on "active sales" will be permitted. However, restrictions on passive sales will be treated as "hard core" restrictions considered so serious that their presence in a distribution agreement will prevent the agreement from benefiting from exemption under the draft Regulation.

Accordingly, it is particularly important for suppliers of branded products to know which restrictions they may want to place on internet selling by their distributors will be regarded as restrictions on passive sales. The draft Guidelines prove some examples of such "hardcore restrictions":

- Preventing customers in another territory from viewing their website or automatically to reroute such customers to the manufacturer's or another distributor's website;
- Terminating internet transactions if credit card details reveal an address outside the distributor's territory;
- Limiting the proportion of overall sales made over the internet – though a minimum value or volume of non-internet sales may be imposed; and,
- Requiring a distributor to pay a higher price for products intended to be resold by the distributor online than for products intended to be resold off-line.

However, suppliers may impose quality standards for internet selling and those using selective distribution can require distributors to have a physical shop or showroom before engaging in online distribution.

III. Resale Price Maintenance

There is increased emphasis in the draft Guidelines on the possibility of arguing that "hard core" restrictions not exempted under the draft regulation can nevertheless be exempted under Article 81(3) of the EC Treaty based on their generation of efficiencies. The most striking example of this is the new guidance setting out the circumstances in which fixed or minimum resale price maintenance may be exempted, a possibility that is not even considered in the current Guidelines.

While the draft Guidelines explain the possible negative effects of RPM, they also refer to a number of specific cases where RPM may generate pro-competitive benefits that meet the efficiency standard of Article 81(3).

- RPM may be necessary to introduce a new product or enter into a market based on the theory that temporary RPM will induce retailers to invest in promotional efforts in order to generate and develop demand for the product;
- RPM may also be authorized in franchise systems to coordinate a short-term low price campaign (between 2 to 6 weeks in most cases); and,
- RPM may be necessary to avoid the loss leading brand practices of large retailers.

IV. Purchasing Power of Large Retailers

The EC is concerned at the increased buyer power of large retailers such as supermarkets and other big distribution chains and believes the current 30% market share "safe-harbor" threshold which currently applies only to the supplier's market share does not adequately address the potential anticompetitive effects resulting from restrictions requested and obtained by these large distributors. Accordingly, it proposes that the market shares of both supplier and buyer would be required not to exceed 30% "on any of the relevant markets affected by the agreement" to benefit

from the exemption provided by the Regulation, i.e. the supplier's share of the market it supplies the buyer, and the buyer's share of the market where it resells.

Beyond an individual market share of 30%, distribution agreements would not benefit from the exemption and the parties would need to self-assess the compatibility of their agreement under the strict EU competition rules.

V. Other Proposed Changes

A. Upfront Access Payments

The draft Guidelines also contain new sections on "upfront access payments" and "category management" agreements. Upfront access payments are exempted up to the 30% market share thresholds discussed above. Even above these market shares, the EC recognizes that upfront access payments can contribute to an efficient allocation of shelf space for new products and prevent suppliers from free-riding on distributors' promotional efforts. However, the EC also highlights the risk of anti-competitive foreclosure of other distributors or suppliers and collusion between distributors.

B. Category Management Agreements

Similarly, "category management agreements" under which the distributor entrusts the supplier with the marketing of a particular product category will be exempted up to the 30% market share test. When this does not apply, the EC recognizes that such agreements also lead to economies of scale but also raise the risks of anticompetitive foreclosure of other suppliers and possible collusion between suppliers or distributors.

VI. Conclusion

The EC's proposal, if adopted, would largely continue the EU's unique competition rules governing distribution agreements between suppliers and retailers. The consultation process runs until September 28, 2009, and will determine the EU's distribution rules until June 2020. It is very much in the interests of companies and business organizations to contribute to this debate by ensuring that their particular concerns and needs are considered by the EC and possibly reflected in the final version of the rules.

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