

Delphi

New EU competition rules for distribution agreements from 1 June 2022



Suppliers and resellers must pay regard to the competition rules when drafting agreements for the purchase and sale of goods and services, so-called vertical agreements. Agreements containing unlawful restrictions of competition are not only wholly or partly void, the parties also risk heavy fines.

The competition law assessment is often complex. In order to facilitate this assessment and to create safe harbours for those vertical agreements that are typically considered to be unproblematic from a competition law perspective, the European Commission issues so called block exemption regulations. A vertical agreement drafted in accordance with a block exemption is automatically approved from a competition law perspective, and the parties need not worry about the competition rules.

On 1 June 2022, a new EU block exemption regulation for vertical agreements entered into force (the "Block Exemption").¹ It builds on previous block exemptions but contains several important new features. In some respects, the rules have become stricter while other changes lead to new opportunities for both suppliers and distributors. The Commission has published guidelines² (the "Guidelines") to further facilitate the interpretation and application of competition rules to these types of agreements. The Block Exemption applies to all kinds of vertical agreements including exclusive and selective distribution agreements, agency agreements, franchise agreements and purchasing agreements.

In the following, Elisabeth Eklund, Partner, Helene Andersson and Karin Roberts, Counsels at Advokatfirman Delphi, highlight the most important news and discuss how they can affect business for companies operating in the EU.

1. The changes in a nutshell

The Block Exemption adopted by the European Commission (the "Commission") on the 10th of May this year, reflects to some extent the debate that has been going on since the work with the revisions began. While the most controversial proposals for change are absent, many of the changes nevertheless involve a significant shift in the view of vertical agreements and can be summarized as follows:

- Some changes are introduced to the rules on so-called "dual distribution", i.e. when the supplier competes with its customer, but the Commission did not implement the most far-reaching proposals for amendments.
- For the first time, the Commission identifies the need to protect physical retail against e-commerce rather than the opposite approach. Suppliers are thus given the opportunity to charge higher prices for goods or services intended for e-commerce than for those to be sold in physical stores.
- Digital platforms can be considered as suppliers in the sense of the Block Exemption. A digital platform that mediates purchases between other actors is to be considered as a supplier and thus needs to adapt to the requirements of the Block Exemption.

¹ Commission Regulation (EU) 2022/720 of 10 May 2022 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, OJ L 134/4.

² Communication from the Commission, Approval of the content of a draft for a Communication from the Commission - Guidelines on vertical restraints C (2022) 3006 final.

- Suppliers are now given the opportunity to expand the group of "exclusive distributors". Previously, a supplier could only designate one exclusive distributor within a certain geographical area or for a certain group of customers. The Block Exemption allows suppliers to designate up to five distributors in the same area or to the same customer group and still rely on the benefits of an exclusive dealer network.
- Suppliers can choose to operate exclusive and selective distribution systems in parallel within the EU. Previously, a supplier had to choose one form of distribution but can now operate an exclusive distribution system in one area and a selective one in another.
- Suppliers may prohibit their buyers from selling the contract goods or services on digital marketplaces, such as Amazon Marketplace and eBay. However, they may not prohibit their buyers from using price comparison services. Buyers and their customers must be given the opportunity to make effective use of the internet.
- Suppliers can now demand that certain commitments are passed on down to the next distribution level and, for example, require distributors to guarantee that their customers do not engage in active sales into areas where someone else has been given an exclusive distribution right.
- Some openings are provided for retail price maintenance to be effective and eligible for an individual exemption.

2. Structure of the Block Exemption

The Block Exemption retains essentially the same structure as its predecessors. This means, inter alia, that any restriction of competition not expressly prohibited in the Block Exemption is permissible, provided, of course, that the agreement in question is covered by the Block Exemption. Article 2 of the Block Exemption sets out that the agreements covered by the Block Exemption are automatically exempted from the prohibition of anti-competitive agreements laid down in Article 101(1) TFEU.

As with the previous Block Exemptions, each party must have a market share not exceeding 30 percent on the relevant market for the Block Exemption to apply. If any party has a higher market share, the parties do not enjoy the protection of the Block Exemption and must instead individually assess whether any restriction on competition is compatible with the rule for individual exemptions laid down in Article 101(3) TFEU and thus permissible.

3. "Dual distribution" – what applies when the supplier competes with its customer?

The concept of dual distribution refers to a situation where a supplier sells products (or services) to an independent retailer while the supplier in parallel sells the products, for example, in its own stores.

The Block Exemption is not applicable to agreements between competing undertakings, except in certain specified situations. The Block Exemption allows situations where the supplier and the distributor are competing at the retail level, as long as the agreement is non-reciprocal, i.e. as long as the buyer is not competing with the supplier at the upstream level. If the buyer is competing with the

supplier also at the upstream level, that agreement must instead be assessed under the so-called horizontal guidelines.³

In order for the Block Exemption to protect an agreement between competitors, any exchange of information between them must be either directly linked to the implementation of the vertical agreement or necessary in order to improve the production or distribution of the contract goods or services. More detailed examples of what may be considered necessary for different distribution types are provided in the Guidelines.

Today, it is common that retailers in certain sectors sell goods also under their own brand. For these situations, the Commission has now introduced a specific rule in the Guidelines. According to this rule, retailers that do not manufacture the private label goods themselves, but outsource such production, are not considered manufacturers of such own-brand goods. This in turn means that they are not considered to compete with suppliers of competing branded goods.⁴ However, if they have their own manufacturing in-house they are considered as competitors.

4. Hardcore restrictions

4.1 The ban on hardcore restrictions is not absolute

Article 4 of the Block Exemption lists hardcore restrictions of competition. The main rule is that the buyer should be completely free to choose its own customers and set its sales price. Contractual clauses which impose such restrictions are considered hardcore restrictions of competition and are therefore blacklisted. However, the ban is not absolute.

4.1.1 Exclusive distribution – up to five resellers

One of the novelties of the Block Exemption is the concept of "shared exclusivity" for up to five resellers in a certain territory or for a certain group of customers. For the exclusive distribution system to be covered by the Block Exemption, the designated resellers must be protected from active sales, i.e. targeted sales efforts, from other distributors.⁵ Just like previously, all prohibitions on so-called passive sales to the exclusive territory or the exclusive group of customers are strictly prohibited.⁶ Distributors may also be prohibited from selling the contract products to unauthorised distributors in the areas where the supplier is engaged in selective distribution. The concepts of active and passive sales are now defined for the first time in the Block Exemption. A further novelty is that the supplier may require that the active sales restriction be "passed on" to the distributor's customers.

³ Guidelines on the application of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements (2011/C 11/01) which, in turn, are currently under review by the Commission. On 1 March 2022, the Commission published its proposals for new horizontal guidelines. The proposals are now subject to a public consultation and new guidelines are expected to enter into force on 1 January 2023.

⁴ Paragraph 92 of the Guidelines.

⁵ Active sales are defined in the Block Exemption as active customer contact through visits, letters, emails, calls or other forms of direct communication or through targeted advertising and marketing; offline or online, for example through print or digital media, including: online media, comparison shopping services and search engine advertising targeting customers in specific areas or groups of customers, the operation of a website with a TLD corresponding to specific areas, or the provision on a website of languages which are widely used in specific areas but which differ from those commonly used in the area in which the buyer is established.

⁶ Passive sales are defined as sales in response to spontaneous inquiries from individual customers, including the delivery of goods or services to the customer without the sale having been initiated through active customer contact regarding a particular customer or group of customers or area; and including sales resulting from participation in public procurement or responses to private calls for tenders.

4.1.2 Selective distribution

Selective distribution is often used for luxury products or for technically complex products. In a selective distribution system, the supplier undertakes to sell the contract goods or services only to distributors selected on the basis of specified criteria. Those distributors undertake not to sell such goods or services to unauthorised distributors within the territory reserved by the supplier to operate the system. The supplier may also restrict the active sale of the members of the selective distribution system (and their customers), to another territory or to a group of customers reserved to the supplier or allocated by the supplier to one or more exclusive distributors. This allows the supplier to protect its exclusive dealer system in another territory.⁷

4.1.3 Requirements for the right to effective use of the internet for sales and advertising

Restrictions which are in any way aimed at preventing distributors or their customers from *using the internet effectively* for the sale and advertising of the goods or services are considered as hardcore restrictions of competition. The Commission provides examples of situations where an agreement can be considered to aim at restricting the effective use of the internet. This applies, for example, to contracts aimed at significantly reducing the overall volume of online sales or seeking to limit the ability of end-users to purchase the goods or services online. The prohibition of the use of digital marketing channels or price comparison services is also considered a hardcore restriction.⁸ However, distributors may be prevented from using digital marketing platforms.

A requirement for the retailer to pay a higher price for products intended for e-commerce than for those intended for sale in physical stores, so-called double pricing, has until now been considered a hardcore restriction. This previously so strict assessment is now more relaxed.⁹

5. Excluded restrictions – individual clauses not covered by the Block Exemption

Non-compete obligations are not in themselves unlawful but may not be concluded with a duration exceeding five years. The Guidelines now state that even non-compete clauses that are tacitly renewable beyond five years can benefit from the Block Exemption as long as the buyer can effectively renegotiate the clause or terminate the agreement before the end of the five-year period. The supplier is still prevented from requiring post-term non-compete obligations. The exception to this ban is franchise agreements. Furthermore, as in the past, members of a selective distribution system must be able to sell the brands of competing suppliers.

A novelty concerns so-called parity clauses. Purchasers of online intermediation services shall not be prohibited from offering more favourable conditions to end-users through competing online intermediation services.

6. Closing remarks

The amendments mean that most companies need to review their distribution agreements to ensure that they continue to enjoy the protection of the Block Exemption, and if not assess whether they qualify for an individual exemption. Some changes will be necessary, others may perhaps imply an opportunity for the parties to better design the agreements according to their needs and preferences.

⁷ Article 4(c) of the Block Exemption.

⁸ Article 4(e).

⁹ Paragraph 209 in the Guidelines.

For the agreements already in force, a transitional grace period of 12 months applies. Thus, by 31 May 2023, companies must revise existing agreements to bring them in line with the new regulatory framework. In other words, it is high time to start the inventory of existing agreements and consider what opportunities the new rules offer for the future.