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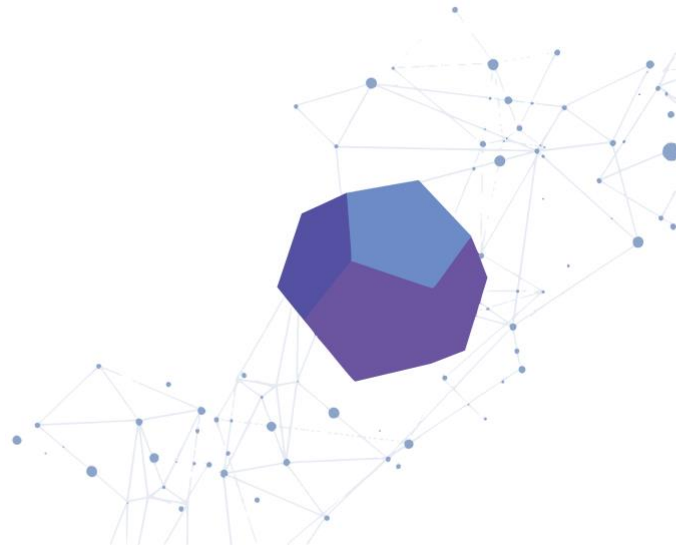

European Commission confirms final texts for new EU rules for vertical agreements

On 10 May, the European Commission (the '**Commission'**) published final texts of the new Vertical Agreements Block Exemption Regulation ('**VBER'**) and the accompanying Guidelines on Vertical Restraints ('**Guidelines**'). These two documents set out the full legal framework for the assessment of vertical agreements under EU competition law that will apply from 1 June.

Although the process leading up to this moment started back in 2018, this means that businesses and their advisers have been given only three weeks to digest the final texts before they come into force. While the main changes that will come into force on 1 June are largely as previewed in the draft texts that were published for consultation back in July last year, there are some surprises.

Background

The VBER creates a safe harbour, known as a 'block exemption', which protects common forms of distribution agreements from legal challenge under Article 101 of the Treaty on the Functioning of the European Union ('**TFEU'**), which prohibits anticompetitive agreements, and equivalent national rules. In principle, any agreement between parties operating at different levels of the supply chain (for example, a brand and a distributor) can benefit from the block exemption's safe harbour, provided that the parties' market shares do not exceed 30% of the relevant markets and the agreement does not contain any 'hardcore' restrictions of competition such as resale price maintenance ('**RPM**'), absolute territorial protection, online sales bans or customer allocation. If an agreement contains a less serious 'excluded restriction', the specific restriction will be taken out of the VBER safe harbour and thus become vulnerable to challenge, but the rest of the agreement will be protected.

While agreements between competitors are in principle excluded from the safe harbour, there is an exception for situations where a manufacturer simultaneously

sells through independent distributors and direct to end customers, in competition with its retail channel (known as 'dual distribution').

The Guidelines set out extensive guidance on application of the VBER and assessing the legality of agreements outside of its protective scope. Taken together, the VBER and Guidelines effectively create a complete code for the application of EU competition law (and, by extension, national competition laws of EU Member States) to vertical agreements.

Proposed changes

As noted in our previous briefing on the Commission's draft texts, following an extensive review of the existing regime for vertical agreements, the Commission proposed a number of changes. These were largely designed to take account of market developments since 2010, when the outgoing VBER entered into force.

Overall, these changes are expressly intended to address what was viewed by some as the outgoing VBER's overly generous approach towards online retail. While this had been justified by the Commission back in 2010 by the need to encourage what was then a nascent e-commerce sector, as a means of driving forward the EU Single Market and improving consumer access to products on a cross-border basis, the political tide has now turned against online retailers. In the current environment, where large online retailers are thriving and high street shops are vanishing, the Commission has thus explicitly shifted the playing field back towards brands and 'brick and mortar' physical retailers.

In summary, the following are the key changes proposed by the Commission:

- tightening the rules regarding the exchange of competitively sensitive information between parties in a dual distribution scenario, to apply a new 10% market share threshold under which such exchanges are covered by the safe harbour. Where parties' market shares are between 10% and 30%, such exchanges would not be protected by the safe harbour, even if the overall agreement is;

- widening the protection afforded by the dual distribution exception so that it applies to situations where there is competition between the supplier and buyer at the wholesale, import or retail level, not just at the retail level, as long as there is no competition between them at the upstream level on which goods are purchased;

- allowing suppliers to appoint more than one exclusive distributor to the same territory or customer group ('shared exclusivity', which was not previously permitted under VBER), as long as the number of distributors appointed is

proportionally related to the allocated territory or customer group, in such a way as to secure a certain volume of business that preserves their investment efforts;
- allowing suppliers that sell through exclusive distribution to require that their customers impose resale restrictions on their own customers ('flow through' of restrictions);

- extensively rewriting the section of the VBER setting out hardcore restrictions to improve clarity;

- removing online platforms (notably Amazon) that operate a hybrid retail and marketplace business model from the protective scope of the VBER altogether;

- allowing suppliers to charge their customers different wholesale prices depending on whether the products are subsequently resold online or offline (a practice known as 'dual pricing', which until now has been treated as a hardcore restriction);

- permitting suppliers that sell through selective distribution to impose selection criteria for online sales that are not equivalent to their criteria for offline sales (also a hardcore restriction under the current regime);

- clarification of how 'online intermediation services providers' such as Amazon, eBay or Booking.com are to be treated under VBER, namely as suppliers of such services to their business customers, which use those services to sell to their end customers;

- limiting the scope of online platforms to rely on the 'genuine agency' exception, which removes sales sold under an agency model from competition law (subject to certain conditions);

- defining retail parity obligations that require users of an online platform not to offer their products on more favourable terms on other platforms as excluded restrictions;

- confirming that (as confirmed by the European Court of Justice in the *Coty* case) the VBER safe harbour applies to total or partial bans on the use of marketplaces;

- updating the Guidelines to make it clear that bans on the use of price comparison sites and online advertising will generally be viewed as a hardcore restriction of competition, as well as reordering the structure to improve clarity; and

- updating the definitions of active and passive sales to make it clear that a supplier operating exclusive distribution can prevent distributors from setting

up a website in the language of a country that is different from that of their home country or from using a different web suffix.

Final texts

Overall, the final texts of the VBER and Guidelines that were published on 10 May follow the drafts published last year. There are some key improvements, however.

First, having clearly taken account of unfavourable consultation responses (including one submitted by this firm), the Commission has removed the 10% market share for information exchange in dual distribution and replaced it with additional guidance on the circumstances in which such exchanges will be permitted. This is a big improvement, as the previous proposal created material additional complexity for little benefit, whereas the new guidance takes a pragmatic and helpful approach that permits any such information exchange as long as it is either directly related to implementation of the agreement or is necessary to improve the production or distribution of the contract goods or services. A new section has been added to the Guidelines to provide guidance on the circumstances in which these tests are likely to be met.

In another sign that it had listened to feedback, the Commission has replaced the vague and subjective test that had been proposed for calculating the maximum number of distributors permitted under shared exclusivity with a simple to enforce numerical limit of five.

In a more surprising development, the Commission has added an entirely new hardcore restriction in Article 4, namely the "prevention of the effective use of the internet by the buyer or its customers to sell the contract goods or services". It is unclear why the Commission (or Member States) felt this was needed, since this was already covered by other parts of Article 4. Indeed, the new Article 4(e) itself states that such a restriction is classified as hardcore because "it restricts the territory into which or the customers to whom the contract goods or services may be sold within the meaning of points (b), (c) or (d) [of Article 4]". The new Article 4(e) goes on to state that this is without prejudice to the possibility of imposing on the buyer "other restrictions of online sales" or "restrictions of online advertising that do not have the object of preventing the use of an entire online advertising channel". The dividing line between "preventing effective use of the internet" or "preventing use of an entire online advertising channel" and imposing "other restrictions" on online sales or advertising is bound to become a hotly contested one in practice.

In another surprise, the Commission has added an entirely new article to the new VBER. The new Article 6 states that the Commission may withdraw the benefit of the VBER safe harbour from an agreement whose effects are incompatible with Article 101(3) TFEU (essentially, where the agreement does not deserve protection). It goes on to state that this may arise in online markets where 'narrow' MFNs are prevalent. Again, inclusion of this new article is mysterious, given that the

Commission (and Member State authorities) have always been able to take such action, under Regulation 1/2003. To date, however, they have never done so. Perhaps adding this new article suggests that they will actually do it in future, or perhaps it is merely making another empty threat more loudly. Time will tell.

The Commission has made a large number of changes to the Guidelines, which are now 105 pages long. While most of these changes are largely cosmetic, and presumably reflect an extensive redrafting process involving many players, some are more significant.

One notable change, albeit more for confirmation that there has been no change in the Commission's approach is a new paragraph on Minimum Advertised Price policies. Following some confusion over the wording of the relevant part of the draft Guidelines, which suggested to some a loosening of the Commission's approach to such policies (which place limits on the circumstances in which buyers may advertise retail prices online). The new wording makes it clear that this will continue to be viewed as a form of indirect RPM.

The final Guidelines also include a new passage on sustainability, no doubt reflecting the increased political interest in this priority objective of the EU. That said, the guidance adds very little of substance, simply noting that qualitative criteria in a selective distribution agreement "may refer to the achievement of sustainability objectives, such as climate change, protection of the environment or limiting the use of natural resources" and that non-compete obligations lasting more than five years that are justified by reference to sustainability objectives may be exempted under Article 101(3). On the former point, it is worth noting that the outgoing VBER already gave suppliers significant flexibility within the safe harbour to set criteria how they wished, including with respect to sustainability objectives, so this adds very little.

One aspect of the Guidelines where the lack of any significant changes is important to note is the passage on marketplace restrictions. As was already the case with the draft Guidelines from last summer, it is clear under the final text that restrictions on the use of online marketplaces by buyers to resell the contract products are not hardcore and are thus block exempted. This remains the case even where the supplier allows some buyers to use marketplaces while prohibiting it for others, or even where the supplier reserves the use of marketplaces to itself. While such facts may lead the Commission to disapply the VBER safe harbour, this has proved to be an empty threat in practice.

Next steps

The new VBER and Guidelines will enter into force on 1 June 2022 and are set to remain in force until 31 May 2034. The new regime will apply to new agreements from that date, while parties to agreements that comply with the current rules will have until 31 May 2023 to make them compliant with the new rules.

Whether the market context will have changed sufficiently in the next 12 years to require such a significant rewrite as this one has proved remains to be seen. There is a risk that the Commission's deliberate policy choice of favouring brick and mortar

retail and exclusive distribution over online retail, including by increasing suppliers' lawful options to limit cross-border sales, may lead to increased segmentation of the Single Market. This may take time to become clear. What is already clear is that, notwithstanding the additional flexibility created under the new VBER and Guidelines, online sales restrictions will continue to be an enforcement focus (as shown by news of dawn raids in the fashion sector only days after publication of the texts). As a result, suppliers will still need to take care that restrictions they place on their resellers' online sales and advertising do not slip into preventing those resellers' "effective use of the internet".

Postscript

In the meantime, the UK has been working on its own rewrite of the domestic competition law regime for vertical agreements. This was necessary since the UK's post-Brexit regime simply incorporated the outgoing VBER and was thus also set to expire on 31 May 2022.

Broadly speaking, the new UK regime follows the new EU regime. Unfortunately, since the UK is no longer a Member State, it was not privy to the emerging final texts. As a result, while the CMA made an effort to stay close to the new EU regime as it developed, they had to base the new UK regime on the drafts that the Commission published last summer, thereby missing out on the improvements made to the final Commission texts. Such is the price of regulatory autonomy.

Sensibly, the UK Government has elected to review the new UK regime after six years, providing an opportunity to align with the new EU regime or diverge further from it. Time, and no doubt developments in UK politics in the meantime, will tell.

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Meet the Authors

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