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The European Commission's draft Regulation and Guidelines on vertical agreements: towards a new and more restrictive Competition Law that nevertheless includes some significant openings

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On 22nd and 28th July 2009, the European Commission firstly presented a draft for the future regulatory framework governing competition in the motor-vehicle sector and, secondly, outlined in a much broader way the new legal environment it is envisaging for all vertical restrictions on competition and, in that respect, of course, for distribution contracts, by publicly announcing its "*vertical restrictions*" package.

In doing so, the Commission's double objective is to close its consultation procedure by submitting its draft texts to public consultation until 28th September 2009 and to prepare economic operators for the new provisions which will become applicable when EC Regulation N° 2790/1999 of 22nd December 1999 expires.

On that date, that is to say on 31st May 2010, the new Community Regulation on vertical restrictions will come into force, with the Commission's traditional guidelines which, as the Commission itself specifies, are designed to *"help companies to make their own assessment of vertical agreements under the EC competition rules".*

The new Regulation and the Guidelines coming with it should certainly be quite similar to those we know today, but they will have new features important to Competition Law practitioners and to companies whose conditions of validity of their vertical agreements, of distribution in particular, will evolve notably on certain aspects.

Motor vehicle EC Regulation Nº 1400/2002 should also end on 31st May 2010, although the Commission is hoping to extend its duration for two years. Conversely, an immediate application of the new general Community Regulation on the vertical restrictions of the so-called after-sales market (spare-part distribution, after-sales services and repairs), where competition appears clearly less vigorous, is envisaged.

Thus, by 1st June 2010 we should have the following two categories of regulatory provisions regarding vertical competition restrictions:

- a general Regulation applying homogeneously to all vertical restrictions, including the after-sales services in the motor-vehicle sector (repairs and spare parts);

and,

- an unmodified Regulation for the primary market covering the sale of new vehicles, which should be maintained for two years before the whole of the motor vehicle market switches to the magnetic field of the general Regulation on vertical restrictions. Specific provisions will then certainly be attached to the general Regulation through a sectoral communication or regulation, according to the Community officials in charge of this matter and to the Commission's communications.

In that context, what are the main thrusts of the projects proposed by the European Commission regarding principally the projected revision of the general Community Regulation?

The principal innovations of the projects published by the Commission to date are as follows:

I. PRESENTATION OF THE FUTURE FRAMEWORK OF EC COMPETITION LAW BY 1ST JUNE 2010

When examining the project of Community Regulation and guidelines on supply and distribution agreements, we have to admit that the Community law on distribution should not be radically changed.

There is certainly no question of an upheaval in the rules applicable to vertical restrictions.

It had been envisaged, and even feared, that there might be radical changes concerning sensitive matters such as Internet selling or exclusive distribution, but we are witnessing a *status quo*, even if the Commission's guidelines give precise details, providing sometimes much more flexibility or greater strictness. We shall comment on those details further on.

Ultimately, the true innovation introduced by the Regulation was unexpected and consists, in future, of taking account of the purchasing power of the buyer, that is to say usually of the distributor.

Where flexibility had been expected (or hoped for) regarding the market share thresholds, we find an important additional requirement in order to benefit from the block exemption, namely that the buyer's market share must be lower than 30%. A number of agreements are therefore going to lose their entitlement to a block exemption solely for that reason, whereas it was on the contrary the increase of the market share threshold of the supplier which was wished, more particularly as regards selective distribution.

We shall summarise below the main points of this new state of affairs.

I.1. <u>The principal innovations announced by the European Commission</u>

I.1.1. The introduction of a double market share threshold

We remember that the present article 3 provides that the block exemption shall apply only on condition that the market share held by the supplier does not exceed 30% of the relevant market on which it sells the contract goods or services.

It is only when an agreement is of "*exclusive supply* ", i.e. when it requires the supplier to sell only to a buyer within the Community, that is taken into account the market share held by the buyer, which must not exceed 30% of the relevant market on which it buys the contractual goods or services.

Now, the Commission considers that two major trends marked the decade following the entry into force of the present rules, that is to say not only the sales on the Internet, which will be considered in a second place (see I.1.2.), but also the constant increase in the purchasing power of the large-scale distribution.

This is why, in order to take account of this substantial development, the Commission is proposing to grant the benefit of a block exemption only to agreements entered into between a supplier and a buyer or distributor whose respective market shares do not exceed 30%.

Thus, article 3 of the draft Regulation is worded as follows:

> *« The exemption provided for in Article 2 shall apply on condition that the market share held by each of the undertakings party to the agreement does not exceed 30% on any of the relevant markets affected by the agreement.* »

The modification which must thus be brought to article 3 of the Community Regulation by creation of this new article 3 specifically dedicated to *"market share thresholds"*, represents a major innovation in the policy on Competition since, whatever the concerned vertical restriction may be, it will be necessary for each of the parties to the agreement not to exceed 30% of the market share.

> ➔ **Only the situation where the market share of both parties would be less than 30% could benefit from the block exemption!**

In order to be convinced that the European Commission is determined to make this modification, it is enough to read the guidelines and particularly the following points about market share thresholds:

- Point 83:

« *Under Article 3 of the Block Exemption Regulation, it is the market share of both the supplier and the buyer that are decisive for the application of the block exemption.* ***Both the market share of the supplier, on the market where it sells the contract products to the buyer, and the market share of the buyer, on the market(s) where it (re)sells the contract products, may not exceed 30% in order to be covered by the Block Exemption Regulation.*** » ;

- Point 86:

« *Where a vertical agreement involves three parties, each operating at a different level of trade, their market shares will each have not to exceed the market share threshold of 30% in order to benefit from the block exemption. If for instance, in an agreement between a manufacturer, a wholesaler (or association of retailers) and a retailer, a non-compete obligation is agreed, then the market shares of the manufacturer, the wholesaler (or association of retailers) and the retailer on their respective downstream markets must not exceed 30% in order to benefit from the block exemption.* »

- Point 106:

« *The assessment of a vertical restraint involves in general the following four steps:*

(1) First, the undertakings involved need to establish the market shares of the supplier and the buyer on the markets where they (re)sell the contract products.
(2) If the relevant market share of both supplier and buyer does not exceed the 30 % threshold, the vertical agreement is covered by the Block Exemption Regulation, subject to the hardcore restrictions and conditions set out in that regulation.
(3) If the relevant market share is above the 30 % threshold for supplier and/or buyer, it is necessary to assess whether the vertical agreement falls within Article 81(1).
(4) If the vertical agreement falls within Article 81(1), it is necessary to examine whether it fulfils the conditions for exemption under Article 81(3). »

- Point 148 (concerning exclusive distribution):

« *Exclusive distribution is exempted by the Block Exemption Regulation when both the supplier's* ***and buyer's market share does not exceed 30 %****, even if combined with other nonhardcore vertical restraints, such as a non-compete obligation limited to five years, quantity forcing or exclusive purchasing. A combination of exclusive distribution and selective distribution is only exempted by the Block Exemption Regulation if active selling in other territories is not restricted. Above the 30 % market share threshold, the following guidance is provided for the assessment of exclusive distribution in individual cases.* »

- Point 153 (concerning purchasing power):

« ***'Buying power' may also increase the risk of collusion on the buyers' side when the exclusive distribution arrangements are imposed by important buyers, possibly located in different territories, on one or several suppliers.*** »

We can see very clearly here the Commission's determination to include purchasing power in its economic reasoning, and particularly the purchasing power acquired by the large-scale distribution. Indeed, the Community Competition Authorities took notice of mergers which occurred in the last ten years between the large-scale distributors particularly in the food-sector and which led to the creation of "super"-listing groups ("*centrales de référencement*") with enormous purchasing power such as Coopernic, merging the Galec (France), Rewe (Germany), Colruydt (Belgium), Conad (Switzerland) and Coop Italia (Italy) groups.

Besides, it was the fear of the anti-competitive effects induced by this situation which led the Commission, in the new paragraphs 199 to 204 of its guidelines, to refer to the issue of the "*upfront access payments*", aiming precisely at the listing fees enabling a supplier to get access to the shelf spaces of the large-scale distribution:

« *(199) Upfront access payments are fixed fees that suppliers pay to distributors in the framework of a vertical relationship at the beginning of a relevant period, in order to get access to their distribution network and remunerate services provided to the suppliers by the retailers. This category includes various practices such as slotting allowances[1], the so called pay-to-stay fees[2], payments to have access to a distributor's promotion campaigns etc. Upfront access payments are block exempted when both the supplier's and buyer's market share on their respective downstream markets does not exceed 30%. Above the market share threshold the following guidance is provided for the assessment of upfront access payments in individual cases.*

(200) Upfront access payments may result in anticompetitive foreclosure of other distributors, in particular when such payments induce the supplier to channel its products through only one or a limited number of distributors. In this case, upfront access payments may have the same downstream foreclosure effect as an exclusive supply type of obligation. The assessment of this negative effect is made by analogy to the assessment of exclusive supply obligations (in particular paragraphs 190-195).

(201) Upfront access payments may also result in anticompetitive foreclosure of other suppliers if the widespread use of upfront access payments increases barriers to entry for small entrants. The assessment of this possible negative effect is made by analogy to the assessment of single branding obligations (in particular paragraphs 128-137).

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[1] *Fixed fees that manufacturers pay to retailers in order to get access to their shelf space.*

[2] *Lump sum payments made to ensure the continued presence of an existing product on the shelf for some further period.*

(202) In addition to possible foreclosure effects, upfront access payments may facilitate collusion between distributors. Upfront access payments are likely to increase the price charged by the supplier for the contract products since the supplier must cover the expense of those payments. Higher supply prices may reduce the incentive of the retailers to compete on price on the downstream market, while the profits of distributors are increased as a result of the access payments. Such collusion between distributors through the cumulative use of upfront access payments normally requires the distribution market to be concentrated.

(203) However, the use of upfront access payments may in many cases contribute to an efficient allocation of shelf space for new products. Distributors often have less information than suppliers on the potential for success of new products to be introduced on the market and, as a result, the amount of products to be stocked may be sub-optimal. Upfront access payments may be used to reduce this asymmetry in information between suppliers and distributors by explicitly allowing suppliers to compete for shelf space. The distributor may thus receive a signal of which products are most likely to be successful since a supplier would normally agree to pay an upfront access fee if he estimates a low probability of failure of the product introduction.

(204) Furthermore, due to the asymmetry in information mentioned above, suppliers may have incentives to free-ride on distributors' promotional efforts in order to introduce suboptimal products. If a product is not successful, the distributors will pay part of the costs of the product failure. The use of upfront access fees may prevent such free riding by shifting the risk of product failure back to the suppliers, thereby contributing to an optimal rate of product introductions. »

In any case, the creation of this double threshold, expressed in market shares held by the supplier on the one hand and the distributor on the other will make the self-assessment of the vertical restrictions included in distribution contracts even more difficult, since a supplier setting up a distribution network or already owning one, which is usually the case, will have to assess not only its own market share but also the market share of its distributor(s) on their own market. This will not be an easy task and doubts will arise regarding the compatibility of its agreement with EC Competition Law.

In our opinion, such legal uncertainty is contrary to the objective set up by the Commission which is precisely to increase legal certainty, since the approach the European Commission was hoping for at the end of the 1990s with Regulation N° 2790/99 was based on the economic effects when vertical restrictions were assessed; such objectives and concerns must, of course, continue to be taken into account today!

Please note that by strictly applying the double market share which would be introduced, agreements which, today, benefit from the block exemption under Regulation 2790/99 would *ipso facto* find themselves outside the scope of the exemption, thus creating a risk of sentence for the companies that are parties to such agreements. We would thus be very far from the "*safe harbour*" which any block exemption regulation shall introduce.

In that situation, it would then be necessary to undergo the delicate competition balance test in order to seek entitlement to an individual exemption according to the criteria set up in EC Law by article 81§3 of the EC Treaty.

Now, we know that it is very difficult to produce evidence of those pro-competitive points and especially to demonstrate the existence of efficiency gains. The parties concerned will therefore often have to give up the vertical restrictions included in their contract or even revise the economic distribution plan of their products.

In that context, will they be granted a transitional period in order to adapt to the new EC provisions?

Will the new provisions be applicable immediately, such as a blade?

It will indeed be clear that the distribution agreement would fall outside the exemption by category in the following situations:

- **Situation A**: the supplier's market share is of 30% and the distributor's market share is under 30%;
- **Situation B**: the supplier and the distributor both have a market share above 30 %;
- **Situation C**: the supplier's market share is under 30% but the distributor's market share is above 30%.

And that would be the case regardless of the type of distribution network set up:

- Exclusive distribution
- Exclusive supply;
- Selective distribution;
- Franchise.

I.1.2. Online distribution

During the round-table bringing together the consumer and industry representatives in order to consider the question of opportunities and barriers to the development of online retailing in Europe, whose work was put on line on 26th May 2009, economic operators fully understood the Commission's wish to abolish the principal restrictions to Internet use existing today.

In particular, the Commission questioned the working group on the opportunity to maintain the distinction between active sales and passive sales in an exclusive distribution network in the case of business on the internet and clearly raised the question of the barriers inherent in the selective distribution system, asking several revealing questions:

- *Do you think it is in the interest of consumers that a producer can use as one of its selection criteria that its dealers have a brick and mortar shop or showroom to taste / feel / experience the product and thus exclude internet-only-shops from its distribution network?*
- *How would you ensure that the criteria used to select dealers do not bias against their use of the internet by imposing criteria for internet selling which are comparatively more severe than the criteria for sales from the brick and mortar shop?*
- *How would you ensure that selective distribution systems and consequent limitations on internet sales are not used for products the nature of which does not require selective distribution?*
- *How would you ensure that selective distribution systems do not hinder the development of new methods of distribution?*

It had then been feared that the Commission would move into a road of excessive liberalisation and would try to abolish all the barriers to Internet trade.

But the crisis occurred and the Commission clearly opted for a certain prudence.

We report below the conclusions of the Commission during those round-table discussions:

« ***B) Online retailing of goods***

(105) There is a consensus that online sales provide all businesses – including car and luxury industries - with huge commercial opportunities and consumers with huge opportunities for access to a wider range of goods at attractive prices. So the Internet is a new route to the consumer, complementary to other channels.

(106) There is no consensus in relation to business practices which limit online

*distribution. On the one hand, **eBay** and **Which** claim that manufacturers of luxury and more common branded goods unduly hinder the online sales of their selected dealers and that there is a need for an increased level of enforcement action. On the other hand, **LVMH** argues that the limitations inherent to selective distribution - such as the exclusion from the distribution network of the "internet only" players or the prohibition on selected dealers to use platforms such as eBay – are demand enhancing. **Fiat** defends a similar view since it argues that a company should be free to choose the mode of distribution that it regards as the most appropriate and it sees little scope for regulatory intervention.*

(107) There is also consensus that online piracy and counterfeiting is a corrosive factor which limits further development of online retailing. It is obvious that effective authentication of the goods is helpful for free and unrestricted opportunities for online distribution.

(108) Finally, despite significant growth, businesses and consumers engaging in online sales continue to face important regulatory barriers such as, for instance, the rules on IP rights and consumer protection.

(109) As far as the business practices are concerned - and more particularly the points where the participants strongly disagree - their views and submissions so as those of the third parties who participated in the public consultation will be assessed in the context of the ongoing review of the legal regime of vertical restraints (the Block Exemption Regulation and Guidelines on vertical restraints).

*(110) On the regulatory side to tackle piracy and counterfeiting, **eBay** stressed in its submission that "stakeholders need to cooperate in their efforts to fight counterfeits" and gave some examples of cooperation with manufacturers[3].*

*(111) **LVMH** had also mentioned during the meeting that there are some available technologies which might help platforms such as eBay to fight online counterfeiting. Cooperation between stakeholders is possible and can clearly help to enhance online sales. During the meeting it was announced that the two companies would hold bilateral discussions subsequently.* »

As the Commission specified very clearly this time when the public consultation on which we are commenting was put on line, it is necessary on the one hand, to preserve the possibility for consumers to buy products abroad at a good price, which the Internet makes easier, but, on the other hand, to avoid that on-line sales allow some "*Pure Player*" distributors to derive undue benefit from the marketing and promotional operations conducted by distributors which operate a brick-and-mortar shop, this being a form of parasitism which the Commission wishes to control, in order particularly to enable consumers to benefit from better quality services.

What can be said with certainty is that, at this stage of its considerations, the Commission has not modified the present EC Regulation by introducing provisions specific to online sales.

Indeed, it is only through the guidelines that we can see, once again very clearly, the European Commission's wish to maintain the freedom of that form of distribution which, it must be admitted, has become a traditional sales channel.

And this is actually in the definition of active sales and passive sales and in the reiteration of the principle of prohibition of passive sales that we see the new outline of European Competition policy in the Internet field appearing very clearly:

« (52) ***Every distributor must be free to use the Internet to advertise or to sell products. A restriction on the use of the***

[3] *See the section "Fighting Counterfeits and Empowering Consumers in the 21st Century Market" from the paper "Empowering Consumers by Promoting Access to the 21st Century Market- A Call for Action", p. 25.*

Internet by distributors party to the agreement could only be compatible with the Block Exemption Regulation to the extent that promotion on the Internet or sales over the Internet would lead to active selling into, for instance, other distributors' exclusive territories or customer groups. In general, the use of the Internet is not considered a form of active sales into such territories or customer groups, since it is a reasonable way to reach every customer. The fact that it may have effects outside one's own territory or customer group results from the technology, i.e. the easy access from everywhere. If a customer visits the web site of a distributor and contacts the distributor and if such contact leads to a sale, including delivery, then that is considered passive selling. The language options used on the website or in the communication normally play no role in that respect.

The Commission regards for instance the following as hardcore restrictions of passive selling:

- ***requiring a (exclusive) distributor to prevent customers located in another (exclusive) territory from viewing its website or requiring the distributor to put on its website automatic re-routing of customers to the manufacturer's or other (exclusive) distributors' websites;***

- ***requiring a (exclusive) distributor to terminate consumers' transactions over the internet once their credit card data reveal an address that is not within the distributor's (exclusive) territory;***

- ***requiring a distributor to limit the proportion of overall sales made over the internet;***

- ***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.[4].*** »

➔ The Commission is therefore suggesting the following approach:

- Internet sales resulting from active commercial canvassing can be the subject of a competition restriction;
- Sales resulting from the consumer's own initiative cannot be the subject of any competition restriction.

However, Internet sales are not entirely liberalised, since the Commission will tolerate certain restrictions to this kind of trade, that is to say:

- The supplier may impose quality standards for the use of a commercial website, as it would do for a shop, an advertisement or promotional activities in general; this may be relevant in particular for selective distribution;
- The supplier may require its distributors to have a brick and mortar shop or a showroom before engaging in online distribution (point 54). The case-law of the French Competition Council, which authorised the exclusion of wholly Internet-based distributors in distribution networks and in selective distribution networks more particularly, is thus validated.

Although the Commission also envisages that an outright ban on Internet selling can be authorised where applicable if it is "*objectively necessary*", which might indicate that, in the Commission's mind, the prohibition on Internet selling was not a restriction *per se*, the examples it quotes immediately remove that impression because it refers only to the case of sale of dangerous substances. Apart from the risk to health or safety, it therefore seems very difficult to get a validation of an outright

[4] *« This does not exclude the supplier's offering the buyer a fixed fee to support its off-line or online sales efforts.*» .

ban on Internet, which was indeed refused to a pharmaceutical laboratory, although it presented genuine and convincing arguments to the Competition Council. [5]

Thus, there can be no doubt that a supplier will not be able to reserve Internet sales or advertising for itself or prohibit any Internet sales!

However, in spite of everything, taking a position that is clearly a compromise, the Commission does offer a number of significant flexibilities since, where it specifies that it considers as an hardcore restriction the fact of "*requiring a distributor to limit the proportion of overall sales made over the Internet*" (point 52), it adds in a footnote:

> « *This does not exclude the supplier requiring, without limiting the online sales of the distributor, that the buyer sells at least a certain absolute amount (in value or volume) of the products off-line to ensure an efficient operation of its brick and mortar shop, nor does it preclude the supplier from making sure that the online activity of the distributor remains consistent with the supplier's distribution model (see paragraphs 54 and 57). This absolute amount of required off-line sales can be the same for all buyers, or determined individually for each buyer on the basis of objective criteria, such as the buyer's size in the network or its geographic location.* »

The Commission therefore does not rule out the possibility for a supplier to seek a certain balance between Internet sales and brick and mortar sales in an endeavour to preserve the consistency of its network. However, it is not easy to grasp exactly where the Commission draws the dividing line between the prohibition on limiting Internet sales and the possibility of ensuring effective brick and mortar sales, supported by sales targets, aiming at preserving the "*distribution model*" of the supplier.

In that respect, a few details would not be unhelpful …

Moreover, it would have been preferable if the Commission had issued a clearer overall opinion about Internet sales because, in the end, it is only through simple guidelines which the national competition authorities may use as an assessment guide, as worded by the Competition Council (at the time), that the subject is tackled.

In that respect, why didn't the Commission envisage clear, legible provisions in the Regulation themselves, by setting up a whole article dedicated to on-line trading, since on-line trading is definitely one of the distribution channels the most frequently used by consumers nowadays?

Having said that, the Commission also provides a very innovatory exception to the prohibition to limit passive sales, including Internet selling, by stating in point 56 of its guidelines:

> « *A distributor which will be the first to sell a new brand or the first to sell an existing brand on a new market, thereby ensuring a genuine entry in the relevant market, may have to commit substantial investments to start up and/or develop the new market where there was previously no demand for that type of product in general or for that type of product from that producer. Such expenses may often be sunk and in such circumstances it could well be the case that the distributor would not enter into the distribution agreement without protection for a certain period of time against (active and) passive sales into its territory or to its customer group by other distributors.* ***Where substantial investments by the distributor to start up and/or develop the new market are necessary, restrictions of passive sales by other distributors into such a territory or to such a customer group therefore generally fall outside Article 81(1) <u>during the first two years</u> that this distributor is selling the contract goods or services in that territory or to that customer group.*** **»**.

[5] Decision n° 08-D-25 of 29th October 2008 against which an appeal was lodged.

The Commission thus considers that the launch phase of a new brand or of an existing brand on a new market can justify the protection of territories against passive sales for the first two years. This constitutes a significant change of direction by means of which the Commission, departing from its dogma of restrictions *per se*, takes account of the special features of the launch phases and of the investments they necessarily imply. It would have been helpful if it had also made it applicable to new products … Let us wait for the final version of the guidelines.

* * *

I.2. The other innovations introduced by the draft EC Regulation:

- Redemption of hardcore competition restrictions:

Point 47 of the guidelines specifies that the hardcore competition restrictions defined by article 4 of the Regulation can be redeemed according to a competition balance. The presumption of flagrant incompatibility of this type of competition restriction could thus become more fragile, the Commission imposing on itself the task of "*effectively assessing – and not just presuming - the likely negative effects on competition"* of the hardcore restrictions.

- Imposed minimum prices:

Imposed minimum prices are still firmly prohibited.

However, the imposition of a minimum price or a minimum margin has been since a long time at the heart of numerous discussions, many practitioners having hoped that the Commission would demonstrate some change of direction in its policy.

It seems that (some of) those hopes have been heard. In fact it is important to note that point 221 of the guidelines now provides that resale price maintenance can have effects other than restricting competition and that, quite to the contrary, they can sometimes lead to efficiencies. Isn't it here a nice declaration, and a certain evolution of the reasoning of the European Commission? In that respect, we can refer to an article written by Frédéric Jenny, former vice-chairman of the Competition Council, in the journal of the School of Mines, which already envisaged efficiencies linked to the imposition of a price.

However, until recently the subject has been somewhat taboo!

The Commission has thus opened a breach in the intransigence of the arguments it and the national competition authorities have presented until now.

In view of their importance, we shall quote those provisions of point 221:

> « ***However, RPM (Resale Price Maintenance) may not only restrict competition but may also sometimes lead to efficiencies, which will be assessed under Article 81(3).*** *Most notably, where a manufacturer introduces a new brand or enters a new market, RPM may be helpful to induce distributors to better take into account the manufacturer's interest of developing demand for the product. RPM may provide the distributors with the means to increase promotional efforts and if the distributors in this new market are under competitive pressure this may induce them to expand overall demand for the product and make the entry a success, also for the benefit of consumers. Similarly, fixed resale prices, and not just maximum resale prices, may be necessary to organise in a franchise system or similar distribution system a coordinated short term low price campaign which will also benefit the consumers. In view of the short duration (2 to 6 weeks in most cases) this may not even have any appreciable negative effects. Occasionally, RPM may also be useful to avoid that a large distributor uses a particular brand as a loss leader. This practice of selling below cost as a loss leader will in the short run*

benefit consumers but may also, if the product is de-listed by other retailers, lead to a reduction of inter-brand competition over time to the disadvantage of consumers. »

While opening the door to resale price maintenance, the Commission is also severely injuring the much-used mechanism of recommended prices by considering that maximum and recommended prices may have the same effect as resale price maintenance since they can work as a focal point for resellers and can thus be followed by most or even all of them which might well facilitate collusion between suppliers (point 223).

The same point 223 also describes the third branch of the well-known body of clues in antitrust legislation, that is to say the existence of a mechanism for monitoring recommended resale prices and the introduction of retaliatory measures if distributors fail to meet the recommended prices, communicated or mentioned to them.

The Commission also considers the phenomenon of double marginalisation in the case of maximum resale prices, the purpose of the communication of a maximum resale price being to avoid the "*double marginalisation*" practice (point 103).

This evolution of the EC Competition policy prohibiting resale price maintenance must be placed in the context resulting from the Leegin judgement (Leegin Creative Leather Products Inc. vs PSKS Inc. – 127 S. Ct 2705 (2007)) which was in all the law reports on Competition in 2008, the United States Supreme Court having indeed applied the rule of reason (i.e. article 81-3 TCE in EC law) which principal impact on Competition Law lies in the need to demonstrate that the supplier has a market power on the relevant market where it is developing.

Thus, in the absence of market power, it would be possible for the supplier to fix a minimum resale price for its distributors; this is what the antitrust law resulting from the various decisions issued in the United States, shows us:

"*Antitrust law assumes that '[w]ithout market power, a firm cannot have an adverse effect on competition'*[6]*. Any effort by a firm in a competitive market to raise prices anti-competitively would just lead 'consumers [to] shop around to find a rival offering a better deal'*[7]*.*

The market power requirement will greatly limit the scope of liability for RPM (Resale Price Maintenance) policies adopted by manufacturers. Most consumer goods companies, companies like the Leegin corporation, simply do not have market power. Leegin sells belts, shoes, purses, sunglasses and similar women's accessories for which there are literally countless substitutes. By any reasonable measure, Leegin is a tiny player in an enormously competitive market and has a market share of a few percentage points or less. Nonetheless, prior to the Leegin decision, the company had been found liable for treble damages because the Dr Miles rule per se ignored market power."

The European Commission has not yet reached that point and, if the door is very slightly open, be careful because the opening is extremely narrow and it would be very easy to get one's fingers pinched!

I.3. Other points to be noted in the draft Regulation

- The Regulation still does not refer to the sub-contracting agreements:

The Commission indeed wishes to maintain its position, which is to make such agreements subject to the interpretation given by its Communication on the

[6] *Ezzo's Inv Inc v Royal Beauty Supply Inc, 243 F.3d 980, 988 (6th Cir. 2001)*

[7] *Murrow Furniture Galleries Inc v Thomasville Furniture Indus Inc, 889 F.2d 524, 528 (4th Cir. 1989).*

assessment of sub-contracts in the light of article 81 § 1 of the TCE[8].

Subcontracts, according to which the sub-contractor undertakes to manufacture certain products exclusively for the principal who supplies the subcontractor with specific technology or equipment, are not usually affected by article 81 § 1, provided that the technology and equipment concerned are necessary to enable the sub-contractor to manufacture the products.

However, some limitations on the restrictions imposed on subcontractors, such as an obligation not to use the results of their own research and development work or the fact of setting aside their production for the principal may fall under article 81 § 1 of the TCE (point 22).

- Agency agreements: some useful details

Real agency agreements are not covered by the law on cartels, provided that the agent is a natural person or a legal entity acting in the name and on behalf of its principal, or even in its own name but still in the name of its principal and does not bear any commercial or financial risk in relation to the activities for which the principal appointed him (point 13).

As a general rule, the determining factor which makes the agency contract subject to the law on cartels is thus the commercial or financial risk the commercial or commission agent bears, which must remain negligible.

The Commission has not changed its position on that point, but has added certain criteria excluding the agency agreements from the law on cartels such as the absence of an after-sales or repairs service or of a guarantee, unless the service concerned is fully reimbursed by the principal or is not essential in order to sell or buy the goods concerned (points 14 and 16).

[8] JOC 1 of 3rd January 1979.

In that respect, we shall remember the recent decision handed down by the Competition Authority on 30th June 2009 in the women's ready-to-wear clothing sector.

II. THE MOTOR VEHICLE SECTOR

As indicated in the introduction, two systems should thus exist as from 1st June 2010:

➔ For the primary sector covering the distribution of new vehicles, the present regulation 1400/2002 should therefore be kept as it is for two years in order to guarantee the motor vehicle sector a "*legal certainty and predictability about the future competition system, especially at this time of crisis".*

At the end of this period, the Commission proposes simply to bring the rules applicable to the primary market into line with the general rules in force for all vertical agreements, as those rules will emerge from the future Block Exemption Regulation applying to all vertical competition restrictions, and to introduce a few safeguards in the form of guidelines whose aim will be to avoid any exclusion of new entrants, the imposition of prices ("*tariff discipline*") and the segmentation of the market resulting from territorial protection or barriers to cross-border sales.

The Commission's intention is to ensure a harmonious transition between the present system resulting from a specific Regulation with a long history (Cf. regulation 123/85, followed by 1475/95 and finally 1400/2002) and the general system.

➔ In the case of what is called the after-sales market (the distribution of spare parts and repairs), the general Block Exemption Regulation will be applied as from 1st June 2010, with the addition of sectoral guidelines or even a sectoral exemption Regulation which would be annexed to the present Regulation or would be independent of it.

In that respect, it is interesting to examine the conclusions of the impact assessment report published by the European Commission.

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In the forthcoming months, there is likely to be much discussion and thought on the development of the Community rules on Competition regarding vertical agreements, and as members of the European network of competition law lawyers, the **Antitrust Alliance**, we intend to play an active part, participating closely to the revision of those two Regulations.

We are and shall remain attentive to your reactions and proposals for modifications and are planning to organise a **Competition Breakfast** in the next few weeks devoted to the development of those Regulations.

We shall not fail to keep you informed of the date of this **Breakfast**.