

Review of the Vertical Block Exemption Regulation and accompanying Guidelines on Vertical Restraints

A paper prepared by the European Competition Lawyers Forum¹

The European Commission is currently conducting a review of the Vertical Block Exemption Regulation (“**VBER**”), together with the accompanying Guidelines on Vertical Restraints (“**VGL**”) to determine whether it should let the VBER lapse, prolong its duration or revise it, together with the VGL. In this context, the Commission has asked a number of organisations including the ECLF to identify issues which it considers require clarification in the VGL.²

The ECLF considers that the VGL have generally contributed to legal certainty, providing clear and practical guidance to businesses on how to structure their vertical supply chain arrangements in compliance with Article 101 TFEU. That said, the focus of the VGL remains on well-established sale/resale distribution models in more mature (often offline) markets. The ECLF has identified the following key issues on which further clarification is desirable in order that the VGL reflect new business models and online markets:

- Application of ‘genuine agency’ to online platforms/intermediaries
- Use of narrow vs wide MFNs
- Dual role of market places
- Increased transparency and price monitoring as a result of the use of algorithms
- Brand restrictions
- Platform bans

Application of ‘genuine agency’ to online platforms/intermediaries

The VGL explains that Article 101(1) TFEU does not apply to obligations imposed on a ‘genuine agent’ in relation to the contracts it concludes or negotiates on behalf of the principal. The determining factor is whether the agent bears significant financial or commercial risks or costs in relation to the activities it performs for the principal – where it does so, it will not be a ‘genuine agent’.

There is currently considerable uncertainty as to how to apply the concept of agency to online platforms/intermediaries. A number of European national competition authorities have concluded that intermediaries (specifically, online travel agents) are not ‘genuine agents’ for the purposes of

¹ The European Competition Lawyers Forum (“**ECLF**”) is a group of the leading practitioners in competition law from law firms across the European Union. This paper has been compiled by a working group of ECLF members and does not purport to reflect the views of all ECLF members or of their law firms. The views set out in this working paper also do not necessarily reflect the views of each individual member of the working group or of their law firm. A list of working group members is set out at Annex 1.

² The Commission has asked the ECLF to assume for these purposes that no changes are made to the VBER.

Article 101(1) TFEU; European case law and the VGL also tend to lead to this conclusion. Nevertheless, others consider that platforms are 'genuine agents' and therefore outside Article 101(1) TFEU.

This current uncertainty as to the treatment of online platforms/intermediaries affects the assessment of a number of vertical restraints, including pricing, brand bidding restrictions and MFNs. The ECLF therefore considers that the concept of 'genuine agency' and its application to online platforms/intermediaries is a key area for further guidance in the revised VGL.

Use of narrow vs wide MFNs

The current VGL cover most-favoured nation clauses ("**MFNs**") only in passing, as a means of reinforcing the effectiveness of direct or indirect price fixing when they reduce the buyer's incentive to lower the resale price.³

The ECLF considers that the revised VGL should address MFNs in greater detail for several reasons. First, and most importantly, national competition authorities have expressed divergent views on this topic. A unified position at European level would reduce or even put an end to national inconsistencies and ensure legal certainty. This is particularly important given that, in the online context, companies tend to implement MFN clauses at the EEA or global level. Second, the significant number of cases opened by antitrust regulators in respect of MFNs applied by online platforms such as online hotel bookings or e-books in recent years should give the Commission sufficient background to draw conclusions.

The VGL would benefit from clarification on the effects-based approach taken to assess MFNs. This deeper analysis could consist of the following:

- *A distinction between narrow and wide MFNs* - Wide MFNs require suppliers or retailers to publish the same or better prices and conditions on the relevant third party platform as those published on all other (online) sales channels, whereas narrow MFNs require the same or better prices and conditions as those published on the relevant suppliers' or retailers' own website. Narrow MFNs are usually considered less problematic in light of their procompetitive effects, in particular when they avoid free-riding, and favour investment (see below).
- *Reverse MFNs* - The current VGL only refer to MFNs imposed by a supplier on a buyer. The revised VGL should also address reverse MFNs (i.e. where the restriction is imposed by the buyer (or platform) on the supplier or by the principal on the agent).
- *An analysis of the anticompetitive effects of MFNs* - Anticompetitive effects can be either collusive (i.e. facilitate coordination or dampen competition) or exclusionary (i.e. create barriers to entry or increase the seller's or buyer's bargaining power).
- *An analysis of the procompetitive effects of MFNs* - As recently indicated by the Higher Court in Düsseldorf in the Booking.com case, MFNs can be necessary e.g. "*to ensure a fair and balanced exchange of services between portal operators and hotels*". MFNs can reduce free-riders/opportunism, mitigate hold-up problems, reduce transaction and

³ See VGL, para. 48.

negotiation costs/contractual negotiation delays, or enable creation or improvement of products.

Dual role of market places

Where a company operating an online platform and a producer or distributor enter into an agreement to sell the producer/distributor's products through the online platform, a vertical relationship arises which is largely unaddressed by the current VGL. The ECLF considers that the revised VGL should address this relationship in greater detail - particular areas of concern which should be addressed include:

- *Flows of information* - The online platform will have access to detailed order information (i.e. prices and volumes), and possibly other strategic information (e.g. future planned price changes or new product launches). For the online platform, it is crucial to understand what, if anything, it can legitimately do with this information – this is particularly the case given online platforms increasingly also distribute their own products and may be able to use such information to their advantage (or to assist promotion of competing third party products). For the producer or distributor, it is similarly important to understand what restrictions can be imposed on the flow and use of the information provided to the platform. Neither question is adequately addressed in the current VGL.
- *Intra-brand competition (i.e. between the goods sold on the online platform and those distributed through other channels)* - Certain practices may affect intra-brand price competition. For example, if the online platform is tasked with matching prices offered by other resellers, this may, in practice, eliminate any incentive for these resellers to decrease prices. In terms of non-price competition, the producer/distributor may wish to regulate the channels or marketing tools used by the platform vis-à-vis other resellers (e.g. with a view to focussing the platform's efforts on internet channels and tools, and reserving traditional methods to bricks-and-mortar operators).

Increased transparency and price monitoring as a result of the use of algorithms

Algorithms can increase transparency and the ability to monitor and/or follow prices. A particular area of concern in respect of vertical relationships, on which further guidance is sought in the revised VGL, is the use of algorithms by suppliers to monitor distributors' compliance with recommended resale prices. This may blur the dividing line between legitimate monitoring of distributors' prices and retaliation.

Brand restrictions

The ECLF considers that the application of Article 101 TFEU to brand bidding agreements is an important area for further guidance in the revised VGL. In *Guess*,⁴ the Commission found that restrictions on brand bidding under a selective distribution system were by-object infringements on the basis that (*inter alia*) they aimed to reduce “*the ability of authorised retailers to advertise and ultimately to sell the contract products to customers...and to limit intra-brand competition.*”

⁴ Case AT.40428 *Guess*, 17 December 2018.

While some direction can be taken from this decision, further clarity is required for the following reasons:

- Prior to *Guess*, the ECJ considered in *Coty*⁵ that restrictions on distributors' use of online third party sales platforms were not hardcore restrictions under Article 4(b) or 4(c) VBER. By contrast, in *Guess* the Commission found that brand bidding restrictions fell within the hardcore restriction at Article 4(c) VBER since distributors, while "*in principle able to sell online*", "*were deprived of the ability to effectively generate traffic to their own websites*". However, considerable uncertainty remains as to the treatment of brand bidding restrictions outside a selective distribution system.
- Further, since the Commission's decision in *Guess* the legal test for a restriction by object has received important clarification in the opinion of Advocate-General Bobek in the *Budapest Bank* case.⁶ Of particular relevance to brand bidding arrangements, Advocate-General Bobek's opinion suggests that before a particular form of conduct can be deemed a restriction of competition by object, there should be "*a relatively widespread and consistent practice of the European competition authorities and/or of the courts of the Member States supporting the view that agreements such as that at issue are generally harmful to competition... the Commission stated that the inherently anticompetitive nature of agreements such as the MIF Agreement stems from the judgments of the EU Courts in MasterCard. I would question whether that amounts to the robust and reliable wealth of experience required to support a finding that a given form of conduct is patently and generally anticompetitive.*"

In this context, it is worth noting that the CMA assessed the effects of brand bidding restrictions outside a selective distribution system in its market study into Digital Comparison Tools ("DCTs"). Specifically, while noting that a range of brand-bidding and matching agreements exist between DCTs and their suppliers, the CMA found that narrow restrictions (similar to those imposed in *Guess* and in contrast to 'negative matching' agreements) were the least harmful of the practices observed, with the potential for consumer harm dependent on both the parties' incentives and consumer behaviour.⁷ The CMA concluded that "*it is not clear that the agreements currently have a significant impact on consumers' shopping around and purchasing behaviour in practice even if paid search results are affected*".⁸ Conversely, the CMA found that it was plausible that such agreements may prevent 'free-riding' on brand-owner investments, provide greater clarity to consumers searching for a specific brand, and result in cost-savings on advertising which may be passed to customers.⁹

⁵ Judgement of 6 December 2017, *Coty Germany*, C-230/16, EU:C:2017:941.

⁶ Opinion of Advocate-General Bobek delivered on 5 September 2019 in Case C-228/18 *Gazdasági Versenyhivatal v Budapest Bank Nyrt. & others*, EU:C:2019:678.

⁷ Competition and Markets Authority, Digital Comparison Tools Market Study: Final Report, 16 September 2017, paragraph 4.112.

⁸ Competition and Markets Authority, Paper E to the Digital Comparison Tools Market Study: Final Report, 16 September 2017, paragraph 4.88.

⁹ Competition and Markets Authority, Paper E to the Digital Comparison Tools Market Study: Final Report, 16 September 2017.

In light of the above, further guidance on the treatment of brand bidding agreements would be welcomed.¹⁰

Platform bans

The final issue which the ECLF has identified as requiring clarification in the revised VGL is the treatment of 'platform bans'.¹¹

The current VGL state only that "*a supplier may require that its distributors use third party platforms to distribute the contract products only in accordance with the standards and conditions agreed between the supplier and its distributors for the distributors' use of the Internet. For instance, where the distributor's website is hosted by a third party platform, the supplier may require that customers do not visit the distributor's website through a site carrying the name or logo of the third party platform*".¹² Moreover there is some conflict between this statement and the general stipulation in paragraph 56 of the VGL that online and offline sales restrictions should be "*overall equivalent*".

When the ECJ recently had the opportunity to clarify the law on 'platform bans' in *Coty*, it specifically confined itself to luxury goods and left a situation of considerable divergence between national authorities, particularly Germany and France.

This is therefore a key area requiring clarification in the revised VGL.¹³

¹⁰ It is also worth noting the following research: "Competition and Cannibalization of Brand Keywords", Andrey Simonov, Chris Nosko and Justin M. Rao, 4 September 2015 (the "**Study**"), available online at <https://research.chicagobooth.edu/~media/516A6EE2639F46E0BDA7BE41EC8D8CC3.pdf>. In summary, the Study suggests that the absence of brand bidding restrictions has the overall effect of raising brand owners' search advertising costs. In particular, where competitors also bid on a brand owner's brand name, the resulting paid ads take up more space on the search results page, pushing the brand owner's organic search link further down the page and increasing the rate of cannibalisation by the brand owner's ad of its organic link. This has the overall effect of increasing the brand owner's search advertising spend in circumstances where it does not attract any further customers as a result.

¹¹ i.e. provisions in supply agreements whereby the supplier prohibits its authorised distributors or retailers from reselling the goods on third party online platforms.

¹² See VGL, para. 54.

¹³ It also has implications for the report on Competition Policy for the Digital Era, on which the ECLF is also commenting to the Commission.

Annex 1: Members of the ECLF working group on the review of VBER and VGL

- **Allen & Overy:** Dominic Long
- **Cleary Gottlieb Steen & Hamilton:** Antoine Winckler
- **Sidley Austin:** Stephen Kinsella
- **Slaughter and May:** Philippe Chappatte, Annalisa Tosdevin
- **Uria Menéndez:** Edurne Navarro Varona