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CLIENT ALERT

EU Commission Publishes Draft New Rules for Distribution Agreements: What's to Come for Distribution Relationships in the Digital Age?

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On July 9, 2021, the European Commission published its long-awaited draft of the revised Vertical Block Exemption Regulation (VBER) and Vertical Guidelines. The significant changes proposed by the Commission take into account the specific challenges brought about by the growth of e-commerce and online platforms in the "digital age." The Commission has also taken this opportunity to update and clarify the rules on exclusive and selective distribution, providing businesses with more flexibility to design their distribution system according to their needs.

Businesses distributing goods and services in the EU rely on the Vertical Block Exemption Regulation (VBER) for legal certainty. The VBER and the accompanying guidelines set out the conditions under which distribution agreements are presumed to comply with EU competition law. The current VBER is set to expire on May 31, 2022. Over the past few years, the Commission has been working with stakeholders to assess, update and amend the existing rules to take account of market developments, including the emergence of online platforms and e-commerce (see also our Client Alert of October 26, 2020). The most important changes proposed by the Commission can be summarized as follows:

- **Resale price maintenance (RPM)** (i.e., the practice by which a supplier directly or indirectly establishes a fixed or minimum resale price to be observed by the distributor) continues to be a hardcore restriction under the revised VBER. However, the new draft guidelines include further clarification regarding efficiency justifications for RPM and elaborate on the three examples of an efficiency defense, (already mentioned in the current version of the Vertical Guidelines) namely when a new product is introduced, if there is a short-term low-price campaign, and to avoid free-riding on pre-sale services for complex products.
- **Non-compete obligations** are not covered by the VBER if their duration is indefinite or exceeds five years. However, the new draft VBER would cover tacitly renewable non-compete obligations (i.e., for a period of more than five years) provided the distributor can effectively renegotiate or terminate the agreement with a reasonable notice period and at a reasonable cost.
- **Dual distribution** (i.e., where a supplier sells not only through independent distributors, but also directly at retail level in competition with its distributors) is currently covered by the VBER. However, in recognition of the significant increase in dual distribution in recent years, the revised VBER would only fully exempt vertical agreements between competitors at the retail level when the supplier's and distributor's aggregate market share in the retail market does not exceed 10%. If the supplier and distributor have an aggregate market share of between 10% and 30%, the exemption would apply, but not as regards any exchange of information between the parties: this would have to be assessed under the rules applicable to horizontal agreements. The dual distribution exemption applies not only to manufacturers, but also to wholesalers and importers. However, providers of online intermediation services with a hybrid function (i.e., online platforms that offer products in competition with companies that use the platform to offer products) are excluded from the exemption. Their vertical agreements will have to be assessed on a case-by-case basis.

- **Most Favored Nation (MFN)** or parity clauses (i.e., containing an obligation to offer the same or better conditions to the contracting party as those offered through any other sales channel or the company's own sales channels) are currently covered by the VBER. In recent years, the Commission has seen increased enforcement action in this area and it is in particular concerned about so-called across-platform retail parity obligations. These are parity obligations imposed by suppliers of online intermediation services obliging distributors not to offer, sell or resell to end users under more favorable conditions using competing online intermediation services. These parity obligations are to be excluded from the benefit of the revised VBER and they will need to be assessed individually. All other types of parity obligation, including those requiring distributors not to offer, sell or resell to end users under more favorable conditions when using their own channels, continue to be covered by the revised VBER.
- **Active sales restrictions**: The revised VBER allows active sales restrictions to be passed on to a distributor's customer if the customer has entered into a distribution agreement with the supplier, or with a party that has been given distribution rights by the supplier. This change aims to better protect the investment incentives of exclusive distributors. In addition, the Commission has introduced the concept of shared exclusivity – meaning that suppliers will be able to appoint more than one exclusive distributor in a particular territory or for a particular customer group. The number of possible exclusive distributors will be determined in proportion to the allocated territory or customer group in such a way as to secure a certain volume of business that preserves their investment efforts.
- **Online sales restrictions:** Dual pricing, where the same distributor is charged a higher wholesale price for products sold online than for products sold in a brick-and-mortar shop, has until now been prohibited. Under the revised VBER it will be permitted, as long as the price difference incentivizes an appropriate level of investment and relates to the difference in costs related to the online and offline channels. In addition, the revised Vertical Guidelines no longer requires the criteria in relation to online sales imposed by suppliers in a selective distribution system to be identical to those imposed on brick-and-mortar shops. It will therefore be possible to reflect the fact that these channels are inherently different in nature. Finally, the new Vertical Guidelines codify case law from the EU Court of Justice, in which the Court has acknowledged that a supplier is allowed to prevent its distributors from selling through online marketplaces.

The Commission has invited stakeholders to submit comments on the draft revised rules. Once finalized, the new rules will enter into force on June 1, 2022 and will apply immediately to new agreements concluded after May 31, 2022. Agreements already in force on May 31, 2022 will benefit from a transition period until May 31, 2023, as long as they satisfy the conditions of the current VBER. This transitional period aims to provide businesses with sufficient time to prepare for the upcoming changes.

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