Exclusive distribution

Exclusive distribution : An overview of EU and national case law

Anticompetitive practices, Exemption (block), Distribution agreement, Exclusive distribution, Selective distribution, Foreword, All business sectors

PostScript : Note from the Editors : although the e-Competitions editors are doing their best to build a comprehensive set of the leading EU and national antitrust cases, the completeness of the database cannot be guaranteed. The present foreword seeks to provide readers with a view of the existing trends based primarily on cases reported in e-Competitions. Readers are welcome to bring any other relevant cases to the attention of the editors.

Frank Wijckmans, e-Competitions | N° 68651, www.concurrences.com

Introduction

Compared with the previous overview dealing with exclusive distribution [1], the harvest is small. Interesting caselaw addressing exclusive distribution issues seems fairly rare. This might be a coincidence, but my contention is that it is not. The reduced success of exclusive distribution is to a large extent due to the legal regime advanced by the European regulator since the adoption of Regulation 2790/99 [2]. The objective of this foreword is to provide an understanding as to why businesses seem be to turning away from exclusive distribution and to put the limited caselaw that is available in the appropriate legal context.

What is exclusive distribution?

While traditionally exclusive distribution has been understood very much in line with the concept underpinning Regulation 1983/83 [3], it is striking that practitioners, academics and enforcers (who in many cases probably have not lived through Regulation 1983/83) attach varying meanings to this distribution format. One of the most surprising explanations is the assimilation of exclusive distribution with exclusive dealing. These two concepts may go often hand in hand, but they are quite different. Exclusive dealing concerns the ability of a distributor to handle competing brands and hence touches upon interbrand competition. In the current block exemption (Regulation 330/2010 [4]) exclusive dealing is governed by Article 5 and hence is situated outside the black list. As will be demonstrated below, exclusive distribution concerns essentially intrabrand competition and may raise Article 4, rather than Article 5 issues under Regulation 330/2010.

The current block exemption regime provides that the exclusive rights of the distributor may be territory-related and/or customer-related.
As to the first category, the distributor is granted exclusive territorial rights. This implies that he enjoys some form of territorial protection against competition from other distributors handling the same products and possibly also from direct sales made by the supplier. While often provided for, protection against direct sales does not qualify as a necessary condition for setting up an exclusive distribution scenario. The minimum requirement for such a scenario seems to be that the supplier imposes some type of location clause on all of its distributors. In the absence of such a clause, any distributor remains free to set up shop where he likes and can undermine the territorial protection promised by the supplier to any given exclusive distributor. While the Vertical Guidelines may suggest otherwise, it would not seem strictly necessary to provide, in addition to a location clause, for the imposition of sales restrictions on the other distributors. Again, such sales restrictions may be commonly applied, but they are not an inherent feature of exclusive distribution. Such restrictions must be contractually provided for and do not follow automatically from an agreement being labeled as ‘exclusive distribution’. To suggest otherwise would be hardly tenable given the very strict conditions imposed by the block exemption in respect of such sales restrictions and the fact that the failure to comply with these conditions automatically creates a blacklist scenario (rendering the block exemption inapplicable to the agreement as a whole).

The position seems to be somewhat different for customer-related exclusivity. In exceptional cases (i.e. where the exclusive customer group is situated in a particular location) such exclusivity can be organized through a system of territorial restrictions. For instance, if the exclusive distribution rights concern the spectators of a particular sports or cultural event, a system of location clauses may suffice to ensure that the distributor can enjoy his exclusive rights vis-à-vis that particular customer group. In the vast majority of cases, such a solution will not work as the reserved customer group is spread out and hence can easily be approached by any distributor selling the relevant goods or services. If that is the case, exclusive distribution rights regarding a particular customer group (e.g., supermarket chains or hospitals) will necessitate the imposition of sales restrictions on the other distributors. In the absence of such restrictions, the exclusivity granted to a particular distributor regarding a customer group will be empty. Similarly to territorial exclusivity, customer exclusivity will often be linked with an obligation for the supplier to refrain from direct sales towards the exclusive customer group. However, this does again not follow automatically from the “exclusive distribution” label and will need to be reflected in the contractual terms governing the distribution relationship.

The rise and fall of exclusive distribution

The success of exclusive distribution in the 70s, 80s and the 90s can largely be attributed to the then applicable block exemption regime. As Regulations 67/67, 1983/83 and 1984/83 did not cover selective distribution agreements, the safe harbor of the block exemption was for a long time reserved for non-selective distribution systems. Within those systems, exclusive distribution received both under Regulation 67/67 and Regulation 1983/83 a particularly favorable treatment. On top of all this, the caselaw of the Court dealing with selective distribution did not provide for much legal certainty in cases where the system went beyond the strict criteria for keeping it out of the basic prohibition of Article 101 (1) TFEU.

With the adoption of Regulations 2790/99 and 330/2010 the position has radically changed. Not only do these block exemption regulations provide a fairly generous regime for selective distribution (covering both qualitative and quantitative selectivity and abandoning, for instance, the requirement
that the nature of the products or services must justify the use of a selective distribution formula [8]
), in addition they injected quite onerous conditions into the block exemption regime in relation to
sales restrictions intended to safeguard the rights of an exclusive distributor. From being one of the
champions of the old regime, exclusive distribution downgraded to a rather unattractive alternative
when selecting a distribution format.

Once the shift in approach had been properly understood, businesses started to steer away from
exclusive distribution and selective distribution became the new champion. This fairly radical shift is
also reflected in my own practice. All of the more complicated and interesting distribution
structuring work concerns selective distribution. Work on exclusive distribution still exists, but it has
become rare and typically occurs in less sophisticated distribution environments.

**Exclusive and selective distribution have become twins**

Within the confines of the current block exemption regime, many of the same restrictions can be
imposed irrespective of whether an exclusive or a selective distribution formula is chosen. This is a
point of considerable practical importance. It narrows down the list of differentiating factors that
companies need to consider when making their choice of the most appropriate distribution formula
for their business.

Generally speaking, the black list of Article 4 of Regulation 330/2010 is confined to restrictions that
are imposed on the distributor and does not cover restrictions accepted by the supplier. This means
that, both in the context of exclusive and selective distribution, protection against direct sales by the
supplier can be provided for. The selection of the distribution formula does therefore not depend on
this issue.

In the slipstream hereof, the supplier is free to commit himself not to appoint any other distributor
within a given territory. This boils down to the organization of some form of territorial protection.
Such a restriction obviously applies to the supplier and not to the distributor, and hence it is not
blacklisted. As it does also not appear in the list of Article 5 of Regulation 330/2010, such a
commitment by the supplier is block exempted irrespective of the chosen distribution formula.

The outcome is the same in respect of location clauses. Location clauses are expressly excluded from
the black list. While Regulation 2790/99 was in fact still somewhat unclear on the exact treatment of
location clauses in non-selective distribution scenarios [9], the necessary clarity is now provided in
the introductory part of Article 4 (b) of Regulation 330/2010 [10]. Hence, irrespective of whether
exclusive or selective distribution is chosen, location clauses are deemed compatible with the block
exemption.

Likewise, there is no difference in respect of the ability to impose quality standards. Exclusive
distribution and selective distribution enjoy the same flexibility in this respect. There is no need in
any of these systems for the selection criteria to be uniform, applied in a non-discriminatory fashion
or justified by the nature of the products or services. In that respect, the current block exemption
regime differs substantially from the well-known decision-making practice and caselaw of the past
dealing with cosmetics [11] and watches [12]. This difference should not come as a surprise. While
said caselaw focused on the conditions so as to remain outside the prohibition of Article 101 (1)
TFEU, the block exemption adopts the applicability of Article 101 (1) as its starting assumption. This
is quite logical. A block exemption is only relevant where the conditions for the application of Article 101 (1) TFEU are met and hence there is a need to check the availability of an exemption pursuant to Article 101 (3) TFEU.

Also with regard to the imposition of non-compete obligations (such as single branding), the choice between the two distribution formulas does not offer any particular advantage. The exemption provided for non-compete restrictions in Article 5 of Regulation 330/2010 applies indifferently to both formulas. Admittedly, Article 5(1)(c) contains a specific condition dealing with boycotts in selective systems, but this provision will only very rarely play a role when setting up a new distribution format.

As to the ability to engage in vertical price fixing or issuing recommended resale prices, the block exemption treats exclusive and selective distribution alike. In this area there is again nothing to be gained from choosing the one formula over the other.

**Twins, but not identical twins**

Although many of the restrictions are handled in exactly the same way by the block exemption, there are a limited number of features for which the position is different. These features require particular attention as they will most likely serve as the decisive factors in the selection of the most appropriate distribution formula.

The first issue concerns the source of supply. In an exclusive distribution system, the supplier is able to require that his distributors purchase the relevant products from him or from a source designated by him [13]. This is not so in the case of selective distribution. Selective distributors must remain free to source the relevant products or services from any other player that is admitted to the selective distribution network within the EEA [14]. Hence, the supplier cannot impose himself as the mandatory source of supply.

The second issue concerns the limitation of the ability of the distributor to supply other traders. It constitutes an integral part of a selective distribution system [15] that the distributors must refrain from supplying unauthorized traders. The supplier can (and, in fact, must) keep the system closed. The same is not true for exclusive distribution. Exclusive distributors are in principle free to supply the trade channels (within the EEA [16]) of their choice. As a result, the relevant products or services may end up in the hands of any trader and, even if the supplier disapproves of particular trader profiles, it will not be possible to prevent the exclusive distributor from engaging in selling.

The third important issue deals with the possibility to impose territorial sales restrictions [17]. As to passive selling (i.e. sales made in response to unsolicited orders) the position is the same for both exclusive and selective distribution. With very limited exceptions [18] such passive sales must be accepted by the supplier and cannot be limited or prevented [19]. The failure to do so amounts to a hardcore (black listed) restriction and hence eliminates the application of the block exemption to the agreement as a whole [20].

The major distinction between the two distribution formulas (at least at face value) concerns the ability to prevent active selling. Active selling covers, broadly speaking, any sale that is made due to a (targeted) initiative on the part of the distributor [21]. The basic principle is that, in the context of selective distribution, the restriction of active sales at the retail level is blacklisted [22]. This implies
in practical terms that, even if the supplier has accepted not to appoint any other distributor in the same territory and has imposed a location clause on his network members, marketing by one selective distributor in the territory of another cannot be stopped.

The block exemption adopts a different approach for active sales restrictions that are imposed in an exclusive distribution system. Subject to certain conditions being met, such restrictions are compatible with the block exemption. The relevant conditions can be found in Article 4 (b) of Regulation 330/2010, on the one hand, and in paragraph 51 of the Vertical Guidelines [23], on the other hand. To the extent that a condition stated in the Vertical Guidelines is not duly reflected in the Regulation, one may seriously doubt that it can serve as a valid requirement for the application of the block exemption to a given active sales restriction.

In order to render an active sales restriction compatible with the block exemption (and the Vertical Guidelines), the following cumulative conditions must be satisfied:

- The active sales restriction must apply towards a territory reserved by the supplier (e.g. because he contemplates appointing an exclusive distributor in said territory at a later point in time or he wishes to engage in direct selling in such territory) or towards a territory which has been allocated to a single exclusive distributor. Hence, scenarios of shared exclusivity or where the supplier contractually retains the freedom to appoint additional distributors do not qualify for imposing active sales restrictions.

- The same active sales restriction must be imposed on all of the distributors of the supplier within the EEA. This implies that it does not suffice to restrict active selling by the other distributors that are most likely to become active in the territory of the exclusive distributor (e.g., because they are located in neighboring regions or countries). The Vertical Guidelines require that all of the distributors are subjected to the active sales restriction.

- The supplier is not entitled to require that its distributor limits in any manner the sales by the buyer of the distributor. In other words, if the distributor sells the products to a trader, such trader cannot be restricted in his resale activities. As a result, such trader cannot be prevented from engaging in active selling in the territory of the exclusive distributor. Put differently, the protection against active selling is limited to the level of the distributors of the supplier and does not extend to any other resellers further down the chain.

Practice has learned that these conditions are often difficult to implement. Particularly the second condition presents difficulties, certainly in already existing distribution networks. The price one pays when missing out on any of these conditions is heavy. The active sales restriction turns from a block-exempted provision into a hardcore (blacklisted) restriction. Many companies shy away from active sales restrictions once they have fully understood the conditions and the consequences of the failure to comply with any one of them.

Depending on the circumstances of the case, the ability to impose an active sales restriction will serve at best as a theoretical advantage, but will not be perceived as a practical benefit. The distinction between active and passive selling may raise complicated issues of proof and the conditions to be fulfilled for benefiting from the block exemption are onerous and risky. Together with the possibility to apply an exclusive purchasing requirement, the active sales restriction amounts nevertheless to the most important argument pleading in favor of exclusive distribution. It
should come as no surprise that the persuasive force of this argument is somewhat limited, particularly now that selective distribution can benefit from a flexible block exemption regime.

And outside the block exemption ...

Once the safe harbor of the block exemption is left, one faces the challenge of accomplishing a self-assessment [24] (to justify an individual exemption pursuant to Article 101 (3) TFEU and to demonstrate that there is no abuse of a dominant position within the meaning of Article 102 TFEU) [25]. For a recent example outside of the EEA where exclusive distribution was assessed from an abuse of dominance perspective, [26]. While being popular in legal textbooks, self-assessments are not particularly welcomed in the real world. I have tested the current practice at quite a number of specialized conferences dealing with the rules of EU competition law applicable to vertical agreements and the results, while most likely not statistically solid, are nevertheless striking. The vast majority (+ 90%) of the practitioners attending the conferences concerned confirmed never to engage in a self-assessment exercise with regard to distribution agreements falling outside the block exemption. The vast majority of those who did stated to have rendered only negative advice and never had given a green light on account of a self-assessment. Really no more than a handful of attendees at these various conferences admitted to have come up with a positive outcome of the exercise. The lack of predictability as to how courts may eventually rule on cases falling outside the block exemption may explain why many practitioners deem a self-assessment still a bit of an adventure. Legal practitioners are traditionally not of the most adventurous kind.

Exclusive distribution “passé” ?

It would clearly be an overstatement to suggest that exclusive distribution is “passé”. There are still business circumstances where exclusive distribution may represent the best or one of the best alternatives.

At the same time, it is undeniable that exclusive distribution has lost very much of its favorite status of the past. There are good reasons that explain this evolution:

• The non-availability of a block exemption for selective distribution has driven businesses for several decades in the arms of exclusive distribution. Times have changed and the current block exemption regime has removed this advantage by covering also selective distribution.

• Many restrictions of competition that are typically included in distribution set-ups are treated in exactly the same manner in the block exemption, irrespective of whether exclusive or selective distribution is involved. Hence, also in this respect exclusive distribution cannot claim a particular advantage.

• While exclusive distribution goes often hand in hand with the imposition of territorial limitations (typically, restrictions on active selling), the conditions imposed by the block exemption (in combination with the Vertical Guidelines) are so onerous that the inclusion of such limitations is often avoided. Any mistake in this respect risks bringing the black list (of hardcore restrictions) into play.

• The rise of online selling and the increase in the number of parallel traders steer businesses more and more away from exclusive distribution as this distribution formula permits only limited control
over the distribution channels. Businesses intending to keep their products or services away from parallel traders are naturally turning towards selective distribution. Also the controlled integration of online selling in the distribution set-up is considerably facilitated if selective distribution is chosen. Hence, the current challenges faced by business are in many cases better addressed via selective distribution.

Hence, not entirely “passé”, but clearly less fashionable and in many cases less adapted to the modern distribution needs.


[10] “The restriction of the territory into which, or of the customers to whom, a buyer party to the agreement, without prejudice to a restriction on its place of establishment, may sell the contract goods or services [...]” (emphasis added).


[13] Depending on the proportion the supplier’s products represent in the total volume of the products sourced by the distributor, account may need to be taken of the 5-year limit stated in Article 5(1)(a) of Regulation 330/2010.


With the relatively recent developments in the Swiss enforcement practice, it is advisable to extend the relevant territory to Switzerland. See, Gaba v Gaba International AG and Gebro Pharma GmbH, Wettbewerbskommission, 30 November 2009, available at http://www.weko.admin.ch/aktuell/00.... See also, F. WIJCKMANS and F. TUYTSCHAEVER, Vertical Agreements in EU Competition Law (2nd edn, Oxford University Press, 2011) para 4.32.

Miguel Sousa Ferro, The Lisbon Appeal Court upholds dismissal of private enforcement action that opposed a distributor to a manufacturer in the gas bottle market and provides important general clarifications, 9 April 2013, e-Competitions Bulletin April 2013, Art. N° 57100

Vertical Guidelines, para 55.

See Mario Cistaro, The Italian Competition Authority launches an investigation into a suspected breach of Article 101 TFEU in relation to the supply of nutrition products for wellness and fitness (Enervit), 20 November 2013, e-Competitions Bulletin November 2013, Art. N° 62293

Article 4(a) Regulation 330/2010.

Vertical Guidelines, para 51.

Vertical Guidelines, para 51.

Article 4(c) Regulation 330/2010.

"[…] A territory or customer group is exclusively allocated when the supplier agrees to sell its product only to one distributor for distribution in a particular territory or to a particular customer group and the exclusive distributor is protected against active selling into its customer group by all the other buyers of the supplier within the Union, irrespective of sales by the supplier. […]" (emphasis added).

For an interesting case illustrating the legal uncertainty once the safe harbor environment is left, see Gábor Báthory, The Hungarian Competition Authority invokes cartel rules and leniency policy with regard to an exclusive distribution agreement in the healthcare sector (Kortex/Olympus), 18 December 2007, e-Competitions Bulletin December 2007, Art. N° 15514

