Vertical Block Exemption Regulation – update on dual distribution and information exchange

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The European Commission's Block Exemption Regulation for Vertical Agreements (*VBER*) is the most relevant guidance for the assessment of dual distribution agreements under EU competition law. Together with the accompanying Vertical Guidelines, it shapes the application of the antitrust prohibition to various distribution constellations.

The European Commission (*Commission*) is currently reviewing the VBER and the Vertical Guidelines. In the draft revised rules published last summer, the Commission has proposed significant adjustments with regards to dual distribution. Notably, it has proposed to

- limit the unconditional safe harbour threshold for dual distribution from 30% to 10% market share at retail level;
- exclude all information exchange from the benefit of the block exemption where the parties' combined market share exceeds the 10% threshold;
- exclude those providers of online intermediation services from the benefit of the safe harbour who have a hybrid function; and
- include wholesalers and importers in the exemption.

Many stakeholders criticised the new approach and requested guidance on types of information that can be exchanged between the parties in a dual distribution relationship without risking a cartel infringement. In response, the Commission has proposed to include a new section in the Vertical Guidelines dealing specifically with information exchange in a dual distribution context.

What is dual distribution?

Dual distribution describes a scenario where a supplier sells its goods or services both through an independent distributor and directly to end customers – thus competing with its distributors on the retail market. From a distributor's perspective, suppliers are both partners at the supply level and competitors at the retail level,

whereas from a customer's perspective, they constitute alternative supply options. Due to this hybrid situation, dual distribution can potentially give rise to conflicts of interest and concerns of information sharing. Currently, dual distribution agreements are covered by the VBER provided that the market share of both the supplier and the distributor does not exceed 30% each. With the increase of manufacturers not only selling their products through distributors but also directly over the internet, the Commission has found that possible horizontal concerns between the distributor and the supplier are more likely to occur and that the broad exemption under the current VBER is no longer warranted.

Why were the draft revised rules criticised?

According to the draft revised rules published last summer, a safe harbour applies to dual distribution agreements in scenarios where the retail market share is below 10%. Where the retail market share is above 10% but does not exceed 30%, the VBER applies to dual distribution agreements except for information exchange between the parties. According to the initial proposal, such information must be assessed individually under Article 101 TFEU in consideration of the Horizontal Guidelines.

Stakeholders criticised the 10% threshold as too narrow and costly to calculate. Also, they requested more guidance on the type of information that can be lawfully exchanged between the parties in a dual distribution relationship and on the measures that undertakings can take to address possible competition concerns.

What is the revised proposal and the consultation about?

In the draft new section to be included in response to the public consultation, the Commission deals specifically with information exchange in dual distribution agreements. Information exchange is defined as "any communication of information by one party to the other, irrespective of the characteristics of the exchange". While the Commission acknowledges information exchange between a supplier and a buyer can even be pro-competitive, for instance with regard to the optimisation of production and distribution processes, it finds that it does not benefit from exemption where it is not necessary to improve the production or distribution of the contract goods or services by the parties. The new section is silent on the 10% market share threshold and it is unclear whether this means that this threshold will no longer be part of the final VBER.

What information exchange can benefit from the block exemption?

The new draft includes a non-exhaustive list of examples of information exchange which can generally benefit from block exemption, including:

- Technical information relating to the contract goods or services;
- Information relating to the supply of the contract goods or services;
- Aggregated information relating to customer purchases of the contract goods or services, customer preferences and customer feedback;
- Information relating to the prices at which the contract goods or services are sold by the supplier to the buyer;
- Information relating to the supplier's recommended resale prices or maximum resale prices for the contract goods or services, and information relating to the buyer's actual resale prices, provided that such information exchange is not used to restrict the buyer's ability to determine its sale price or to enforce a fixed or minimum sale price and there is no information exchange relating to actual future downstream sale prices (other than as part of short-term price promotions);
- Information relating to the marketing of the contract goods or services;
- Performance-related information.

What information exchange cannot benefit from the block exemption?

The Commission deems the following examples generally not necessary to improve the production or distribution of the contract goods or services by the parties:

- Information relating to the actual future prices at which the supplier or buyer will sell the contract goods or services downstream, unless the exchange of such information is necessary to organise a coordinated short-term low price campaign;
- Customer-specific sales data, including non-aggregated information on the value and volume of sales per customer, or information identifying particular customers;
- The exchange of information relating to goods sold by a buyer under its own brand name with a manufacturer of competing branded goods, unless the manufacturer is also the producer of the own-brand goods.

This does not mean that exchanging such information amounts to a violation per se. Rather, the information exchange needs to be assessed on a case-by-case basis against the potential justifications described in the Horizontal Guidelines.

How can companies comply?

Finally, the Commission points out that companies can protect themselves against the risk of inadmissible exchanges of competitively sensitive information by

- exchanging only sufficiently aggregated sales information;

- ensuring an appropriate delay between the generation of the information and the exchange; or
- using Chinese walls in order to make sure that the information communicated by the buyer only reaches the personnel responsible for the supplier's upstream activities and is not shared with sales personnel responsible for the supplier's direct sales.

What are the key takeaways?

The Commission's guidance regarding the exchange of information in a dual distribution context is much appreciated. Even though there are no surprises in the concrete examples for permissible vs. potentially problematic conduct, it will be much clearer going forward where safe harbours end. Companies are required to self-assess whether a certain exchange of information is ancillary and not in violation of Article 101(1) TFEU or whether it meets the requirements for individual exemption pursuant to Article 101(3) TFEU. Also, it is comforting that the Commission acknowledges that appropriate ringfencing of information is a legitimate means to reduce competition concerns. If adopted, this could have an impact as well on the Federal Cartel Office's stance in relation to firewalls and other technical means, which sometimes have been considered more of a fig leaf by the agency measure than sufficient risk mitigation.

Still, the Commission could have been clearer on whether it in fact intends to drop the 10% threshold, which would address significant concerns on having to assess an additional complex market share threshold.

The new rules are expected to enter into force in June 2022 when the old VBER is due to expire. Companies engaging in dual distribution are advised to check their current distribution set up in light of the draft new rules. Given that the Commission has now dealt intensively with this topic, it might also shift its enforcement priorities sooner than later. BLOMSTEIN will continue to monitor developments regarding the VBER and Vertical Guidelines closely. If you have any questions on the topic, Anna Blume Huttenlauch, Max Klasse, Marie-Luise Heuer and the entire competition law team will be happy to assist you.