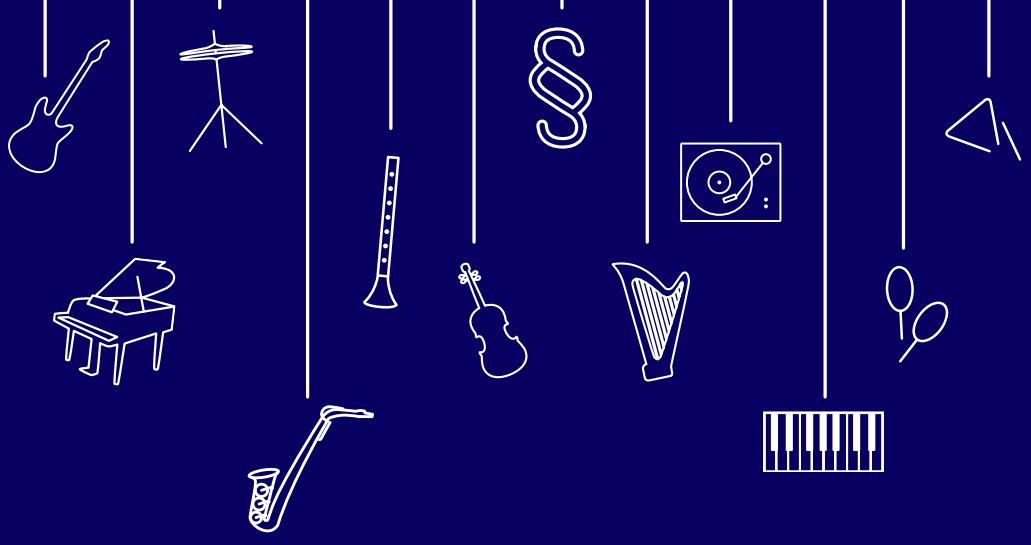
european musical instrument alliance

emia

# VBER Compliance Guidelines

## A Code of Practice – specifically for the MI Industry in Europe



English version


European Musical Instrument Alliance (EMIA) – in alphabetical order:

CSFI

Comusica

DISMA MUSICA

SOMM Society Of Music Merchants e.V.

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# ABOUT EMIA

## Principle

The consititution of EMIA is an important step towards a united and strong European Musical Instrument and Musical Equipment (MI) industry. Four leading national industry associations are joining forces in an alliance to promote the cultural and economic interests of the MI industry in Europe.

The Coalition for the musical instrument industry is an open alliance of leading private-sector interest groups - it sees itself as the competent voice of the MI sector for social and economic change.

As a driving force for politics and government at federal, state and EU level, it develops overarching positions, statements and demands on cultural and economic policy issues. And it aims to harmonise and unite the MI industry in Europe.

The market participants of the MI sector, represented by the Coalition's associations and stakeholders, are the relevant engine for creativity, innovation, productivity and economic growth in Europe, and at the same time a guarantor 'of democracy, diversity and social cohesion.

## The structure

The European Musical Instrument Alliance (EMIA) is an alliance of the major European trade associations of the musical instrument industry (CSFI, DISMAMUSICA, COMÚSICA and SOMM e. V.). It sees itself as a forum and discourse space for relevant national and international associations, industry-partners and organisations, with the aim of identifying, discussing, shaping and optimising the economic and legal framework conditions for all areas of the Musical Instrument industry, and communicating these to political decision-makers.

EMIA is a platform that enables the national associations of the European member states to represent their interests jointly and in a unified manner to policy-makers. EMIA addresses the pressing issues of European politics and defends music as one of the most important assets of our societies.

It is time for all musical instrument associations and companies in Europe to unite and finally speak with one voice in order to be much more representative. United, the sovereign national associations' political demands can be taken into account and the changes necessary for the growth of the market can be implemented, such as competition law, VAT and the enhancement of the cultural role and function of the MI industry in the construction of a new European identity.

EMIA represents the cultural and economic interests of the musical instrument and music equipment industry at national and European level. With the aim of: strengthening the competitiveness of the industry in all market segments, helping to shape the political and regulatory framework in the industry's interests, promoting up-to-date music education and training, and strengthening active music making and music education in society.

## Mission statement

In the world, Europe is considered to be a musical continent, a musical region par excellence. Music and musical instruments are both a cultural heritage and an economic factor. Europe's prospects as a land of music can be measured above all in terms of its potential. The diversity of its cultural heritage, contemporary forms of artistic expression and the cultures of other European countries are at the heart of Europe's cultural diversity and, combined with its geopolitical situation and level of economic development, provide an excellent starting point for exploiting this potential. But all this is at stake. The preservation and development of musical life must remain a commitment for Europe in the future.

## The Vision

Music is part of every person's life - from prenatal to death - and has a major impact on the personal development and shaping of the lives of musicians in particular. It is all too easy to lose sight of the farreaching individual and social effects of making music in purely statistical considerations. For this reason, it is more important than ever, in addition to the numerous studies and scientific evidence on the importance of making music, to re-focus both individuals and society to refocus on the intrinsic value of music and music making. As right as it is to emphasise the indirect and direct effects of making music, it is equally important to bring music for its own sake back into the public consciousness.

### United we're stronger – one voice for the European Musical Instrument sector

**European Musical Instrument Alliance**
Berlin, July 2023

# CODE OF PRACTICE

## A. Guideline's scope

In June 2022, the European Union's revised Vertical Block Exemption Regulation (VBER) came into force. The new VBER and the European Commission's Vertical Guidelines aim to better address new business & distribution models brought about by the digital economy (e.g. online sales, online platforms / marketplaces).

Vertical Block Exemption Regulation (VBER)

The following guidelines are meant to summarise the key changes, ease the pathway to build compliant supplier/distributor relationships and take advantage of the room for manoeuver provided by the new rules for vertical relationships, i.e. to companies active on different supply chain levels. The aim is to bring more clarity to suppliers and distributors, including wholesalers and retailers when building or participating in distribution networks and pricing strategies.

European Commission's Vertical Guidelines

### What's new – in a nutshell

- Under certain conditions,
  - online sales restrictions "specifically targeting online marketplaces" are now possible.
  - supplier may charge different wholesale prices from reseller for products intended to be sold online vs those to be sold offline ("dual pricing").
  - supplier may establish different criteria for online and offline sales in selective distribution systems.
  - active sales can be restricted and may be passed on to direct customers of resellers ("rolling over").
- Suppliers may appoint up to 5 exclusive distributors/resellers per territory/customer group.
- Exemptions concerning resale price maintenance and non-compete clauses are broadened.
- Different distribution systems in different geographical areas now protected from each other (e.g. selected resellers protected from unauthorised resellers).
- Dual distribution exemptions extended to wholesalers and importers.
- More clarity for dual role agents.

## Some ground rules upfront

- Competition law analysis is always driven by the specific circumstances of an agreement and the particular facts at hand incl. specific product features, market conditions, competitive landscape. Therefore, you should always take into account the context of the particular agreement when assessing it. Also bear in mind that competition authorities in some European member states apply these rules stricter than others. If in doubt, please obtain legal advice!
- Market shares play a crucial role in the legal analysis:
  - Where all companies involved in a specific vertical agreement each have market shares **< 30%,** the legal standard is generally less strict, and companies can benefit from **"safe harbours"** (= exemptions).
  - Where at least one company involved has **market shares >30%, the legal standard is stricter:** An individual exemption can apply but a more detailed assessment is necessary, taking into account market conditions, competitive effects, possible efficiencies and the passing-on of benefits to customers.
- Some commercial behaviours are always critical, irrespective of market shares, i.e. even where shares are <30% (so-called **hardcore restrictions).** They are typically not admissible and can even **be subject to administrative fines** *unless justified* due to very exceptional, specific circumstances:
  - Resale Price Maintenance
  - total bans of online channels / Preventions of effective internet use
  - restricting passive sales to certain territories or customer groups

## The following hypothetical case will be used to guide you through the various topics.

**Company C** is a clarinet producer well established in Europe with market shares ranging from 15% to 25% in various member states. The supply of clarinets in the EU is reasonably fragmented among eight other renowned producers, all with moderate market shares.

**C** distributes and sells mainly through brick-and-mortar stores where **C** relies on a large number of small to medium sized specialised musical instruments resellers and also mass merchants, i.e. larger retail chains not specialising only in musical instruments. In addition, **C** increasingly sells through the internet, on its own and in resellers' webshops, including marketplaces.

**To better position itself in the market, C decided to update its pricing and distribution system and to consider the following topics:**

(i) online and offline price differentiation,

(ii) whether to allow the offer of its clarinets in online marketplaces,

(iii) price positioning towards end-consumers,

(iv) whether to rely on an open, exclusive, or selective distribution system, or to adopt a combined approach,

(v) whether if, in parallel to having distribution partners, it should also have its own sales channels.

### Keep in mind

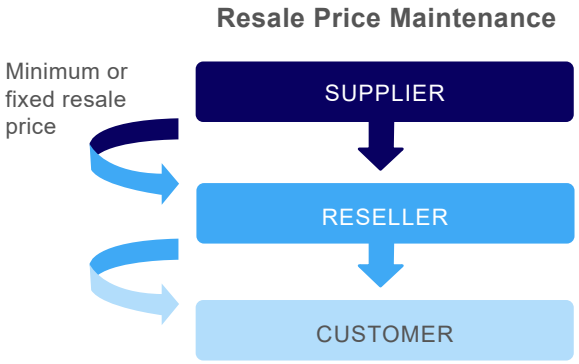
- Since **C's** market share is below the 30% threshold, **C** may benefit from "safe harbours", i.e. a more lenient legal standard when entering into agreements with resellers.
- Purchase decisions for clarinets (as for many instruments) are highly specialised, and brand image is a very important marketing feature.
- Clarinet producers develop products to match different demands of clarinet players relating to proficiency, music style preferences, budget etc.

# B. Pricing

## I. Resale Price Maintenance

**Resale Price Maintenance (RPM)**
= where supplier restricts distributor's ability to determine resale prices by establishing a fixed or a minimum resale price or other measures with similar effects

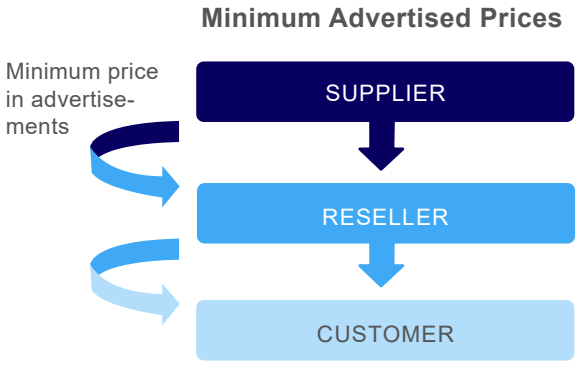
**RPM are hardcore restrictions, i.e. generally not admissible.**




**Minimum Advertised Prices (MAPs)**
= where supplier prevents distributor from **advertising** product below a specified price level

MAPs are not lowest price at which distributor can **sell,** but lowest price distributor can **publicly display.**

MAPs are generally **treated as RPM,** i.e. **generally not admissible (hardcore restrictions).**



## What's allowed for suppliers?

### Admissible

- Recommend resale price ***(RRP)*** and explain price positioning (BUT: must not be *de facto* fixed or minimum price strategy!)
- Impose *maximum* resale price

### Borderline cases: Seek advice!

- Impose maximum resale price or recommend resale price **combined with**

  (i) incentives to apply certain price level (e.g. reimbursement for promotional costs)

  (ii) disincentives to lower sale price (e.g. implementing monitoring systems by supplier or obliging retailers to report deviating members)

**Exemptions under exceptional, specific circumstances and only where supplier has evidence to demonstrate these measures are justified.**

- Set specific or minimum resale price to facilitate **launch / introduction of a new product;** BUT: **only (i) during product's introductory period** (2 to 6 weeks normally acceptable; longer period may be justifiable depending on complexity and life-cycle of product; please seek advice) and (ii) if there is no less restrictive means to incentivise resellers to promote product
- Set specific or minimum resale price to prevent retailer from using supplier's product as **loss leader** ("Lockvogel")
  Loss leader = where reseller intentionally offers certain products at steep discounts, generally below cost, to attract new customers or sell additional products.
- Set specific or minimum resale price to avoid free riding by retailers who do not provide pre-sale services for complex products
- **Franchise Systems:** Set specific or minimum resale price to enable coordinated **short-term** low-price campaigns (2 to 6 weeks)
- **Fulfilment Contracts** (= supplier enters into direct agreement with customer but uses distributor to execute (fulfill) supply obligation): Supplier can set price if distributor is selected by supplier.

### Not admissible

- Fix distributor's resale price
- Prohibit distributor from selling below certain price level
- Request price increase from distributor (and distributor complies)
- Fix distributor's resale margin
- Set maximum discount which distributor can apply
- Condition rebates or reimbursement of promotional costs (or other supply benefits) to observance of RRP
- Link resale price to that of competitors' products
- Use threats, intimidations, penalties, warnings, suspension of deliveries or contract terminations to coerce a distributor to observe supplier's RRP
- Indirectly pressure resellers on resale price by actively monitoring, e.g.

  (i) oblige retailers to report other resellers deviating from RRP

  (ii) implement price reporting or monitoring systems (e.g. price tracking softwares) combined with price compliance incentives (e.g. bonus, rebates)

## Keep in mind

1. Directly or indirectly establishing a fixed or a minimum resale price is generally considered a hardcore restriction of competition (subject to fines!).
2. Exemptions are applicable in exceptional cases and only where supplier is able to prove that exception applies. If you want to claim one of the exceptions, keep record of all relevant documentation (in writing)!
3. Market shares always play a role: The higher the market shares, the more difficult to argue for an exemption!

## Hypothetical case

**Could C set minimum resale prices that retailers should charge for its clarinets?**

No, resellers must be free to determine their own price. However, **recommending resale prices** and **explaining** the price positioning to resellers is ok.

**Could C grant special rebates to retailers who sell its products at the level of the recommended resale price?**

No, such discounts would aim at incentivising retailers to adhere to C's price recommendation, i.e. restrict their freedom to set prices independently. Such discounts would be illegal and subject to administrative fines.

**Would it be ok to implement a minimum advertising price policy whereby C prescribes that all resellers advertise its clarinets above a certain price?**

No, a broad MAP policy applicable to all resellers would not be permissible.

However, if C has concrete evidence to prove that there **is a risk of free-riding** and that C has no other means to address this problem, such a policy could be justified. C would need to be able to show that, for example

- C's brand image benefits from specialised high-service retailers providing end-consumers with pre-sale services and dedicating special display for C´s clarinets in the stores.
- Clarinet buyers often visit brick-and-mortar stores for personalised advice and to test the options but end up buying the product cheaper online from online-only-resellers offering C's clarinets without pre-sale customer services (on their own websites or marketplaces).

## Hypothetical case

**C wants to launch a very innovative, premium new clarinet. Can C communicate a minimum resale price to retailers to make sure that the clarinet's premium quality is perceived in the market correctly?**

Yes, launching a new product is one of the exceptional situations in which a minimum resale price may be justified but only where the following conditions are met:

- C would have to be able to demonstrate that it is necessary (and there are no alternative means) to provide resellers the proper financial incentives to promote the product, for example, to assure proper remuneration of initial investments incurred by retailers with training sales personnel and with product promotion and display.
- Only during a short, limited time period (i.e. the product's introduction period, normally not more than 2-6 weeks; if C has special reasons why a longer time period is needed, C should consult legal advice).

**C has been annoyed with retailer R who systematically prices C's clarinets below wholesale price and uses the clarinets as a "loss leader" in his marketing material in order to attract customers to his stores. Can C prevent R from selling below acquisition cost?**

Yes, if a retailer with a significant market position sells below own acquisition cost, a supplier may communicate a minimum resale price but only where the following conditions are met:

- C can tell R a minimum resale price if this is **primarily aimed at saving C's brand image,** e.g. because C clarinets require high investments in customer services, sales promotion and display, and
- **R holds significant market share** (i.e. at least >35–40%) which means R's pricing strategy could undermine the incentives of other resellers to invest in C's brand image.

**Can C require resellers to provide advance information on planned promotional prices to better prepare for the supply of additional demand?**

This type of information request is risky as it could be considered being an RPM monitoring mechanism (e.g. the German competition authority is critical towards such requests!). However, if a reseller needs supplier's advice regarding anticipated volume effects due to a specific (planned) promotional retail price, retailer should ask for advice based on several possible hypothetical retail price alternatives (i.e. "how would volume increase with Price X, how would volume increase with Price Y, volume increase with Price Z?").

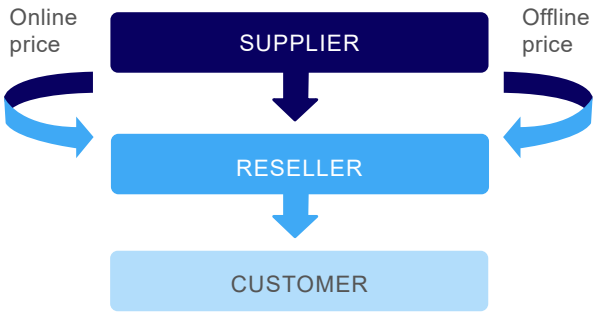
## Hypothetical case

**Can C request from its resellers to provide sales data for its products relating to the penultimate quarter for business management and intelligence purposes (e.g. sales strategy and product planning)?**

Yes, this would generally be admissible if there is a period of at least 3 months between the time of the sale and the delivery of the sales data and as long as data is not used by supplier to monitor RRP compliance. Also, if supplier remunerates reseller for the data provided, it shall have no relation with RPP compliance. As precaution, reseller should make sure in the agreement/email correspondence with supplier that the information provided is not passed on to third parties, namely competing resellers.

## II. Dual Pricing

**Dual pricing** = different wholesale prices are charged from reseller for goods to be sold online vs. goods to be sold offline




**Can be admissible when**

- aim is to **incentivise** or **reward appropriate level of investments,** and
- price differentiation is related to **costs and investment differences between** online and offline sales channels.

*unless* the (real) aim is to prevent **effective use of the Internet as a sales channel** to particular territories or customer groups (hardcore restriction subject to fines!)

### What's allowed for suppliers?

| Admissible | Not admissible |
|---|---|
| • Set different wholesale prices for online and offline sales to incentivise or reward appropriate level of investments<br><br>BUT: price difference must be reasonably related to differences in costs and/or investments between online and offline sales channels | • Apply different wholesale prices with the aim or effect of making online sales unprofitable or financially unsustainable<br>• Use dual pricing strategy as means to limit quantity of products available for sale online (do not cap amount of products that may be sold online!)<br>• Require from reseller that retail prices be higher or lower depending on the sales channel |

## Keep in mind

"Safe harbour" only applies where market share of both supplier and reseller is < 30%. Where market shares are >30%, supplier will need to prove that individual exemption applies (burden of proof! keep record of relevant documentation).

## Hypothetical case

**C supplies a distributor that sells through a combination of offline and online channels (hybrid reseller).**

**Can C charge hybrid resellers a higher wholesale price for identical clarinets for online sales because offline channels are vital in building C's brand image and C wants to discourage resellers from selling online?**

No, this would be illegal because in this scenario the price differentiation is indeed a strategy to make online sales channel less attractive; it could ultimately lead to preventing the effective use of the internet for sales (hardcore restriction!).

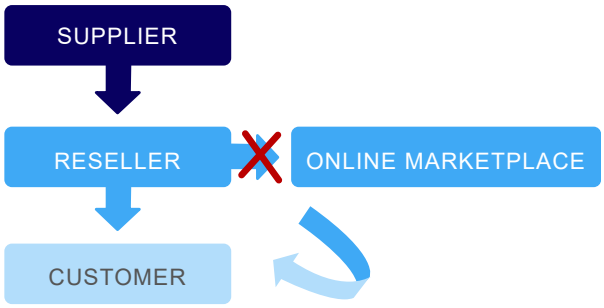
Setting different wholesale prices would only be admissible in a scenario where C wants to reward retailers for their higher level of investments in offline channels, e.g. specifically when the costs and investments incurred for promoting and selling clarinets in brick-and-mortar stores are actually higher than in webshops, the offline wholesale price may be lower. The price variation must be related and proportional to the difference investments and costs incurred by the reseller to make sales in each channel.

To implement dual pricing towards hybrid resellers, a methodology can be agreed that takes into account the ratio between offline and online sale, such as balancing of accounts after the sales are effectively made.

# C. Marketplace bans

**Marketplace bans** = supplier restricts distributor in using (certain) e-commerce platforms/marketplaces

Certain restrictions are possible provided they do not prevent entirely the use of the internet as a sales/advertising channel.




## What's allowed for suppliers?

### Admissible

- Restrict sale on select, specific marketplaces while allowing reseller
  - to sell via its own online store or other online channels (incl. third-party platforms);
  - and to use search engine optimisation (SEO) techniques or advertise online to increase visibility

### Borderline cases: Seek advice!

- Specify qualitative criteria to allow use of (certain) online marketplaces unless this leads to de facto total online sales ban
- Restrict sale on all marketplaces in order to preserve quality and ensure proper use of the products unless there are other means to achieve this goal

### Not admissible

- Totally ban the use of online sales (incl. marketplaces and reseller's own online channels)
- Restrict sale on marketplaces only for some resellers but not for others (discrimination!)
- Restrict sale on marketplace by reseller although supplier itself uses such marketplace
- Restrict sale on marketplace although banned marketplace operator is an authorised member of a selective distribution system

## Keep in mind

"Safe harbour" only applies where market share of both supplier and reseller is <30%. Where market shares are >30%, supplier will need to prove that individual exemption applies (burden of proof! keep record of relevant documentation), specifically that the aim is not to prevent the effective use of the internet for sales.

## Hypothetical case

**Could C ask its distributors not to sell C's clarinets on eBay*?**

Yes, it is possible to prohibit one specific marketplace as long as distributors remain free to sell on other online sales channels, e.g. via their own webshop or other marketplaces, and they are free to advertise their online channels (incl. on search engines) and to use SEO techniques to increase visibility and attract customers.

**Note:** Restriction must be applied equally to C itself and to all resellers on non-discriminatory basis. Otherwise: risk of restricting intra-brand competition (=competition between resellers of the same brand). C cannot prohibit distributors to sell on eBay* while maintaining his own sales of clarinets on the marketplace.

**Could C ask its distributors to only sell C's clarinets on marketplaces that allow distributors to create their own brand shop within the marketplace?**

Yes, C can specify certain criteria that marketplaces should meet in order for C's clarinets to be sold (e.g. in terms of customer service, product presentation) so that C can secure its brand image provided such criteria are aimed at exceptional product and customer service (pre and post-sales) quality.

C could also specify criteria in order to exclude specific marketplaces which do not provide adequate customer services, thereby damaging C's brand positioning.

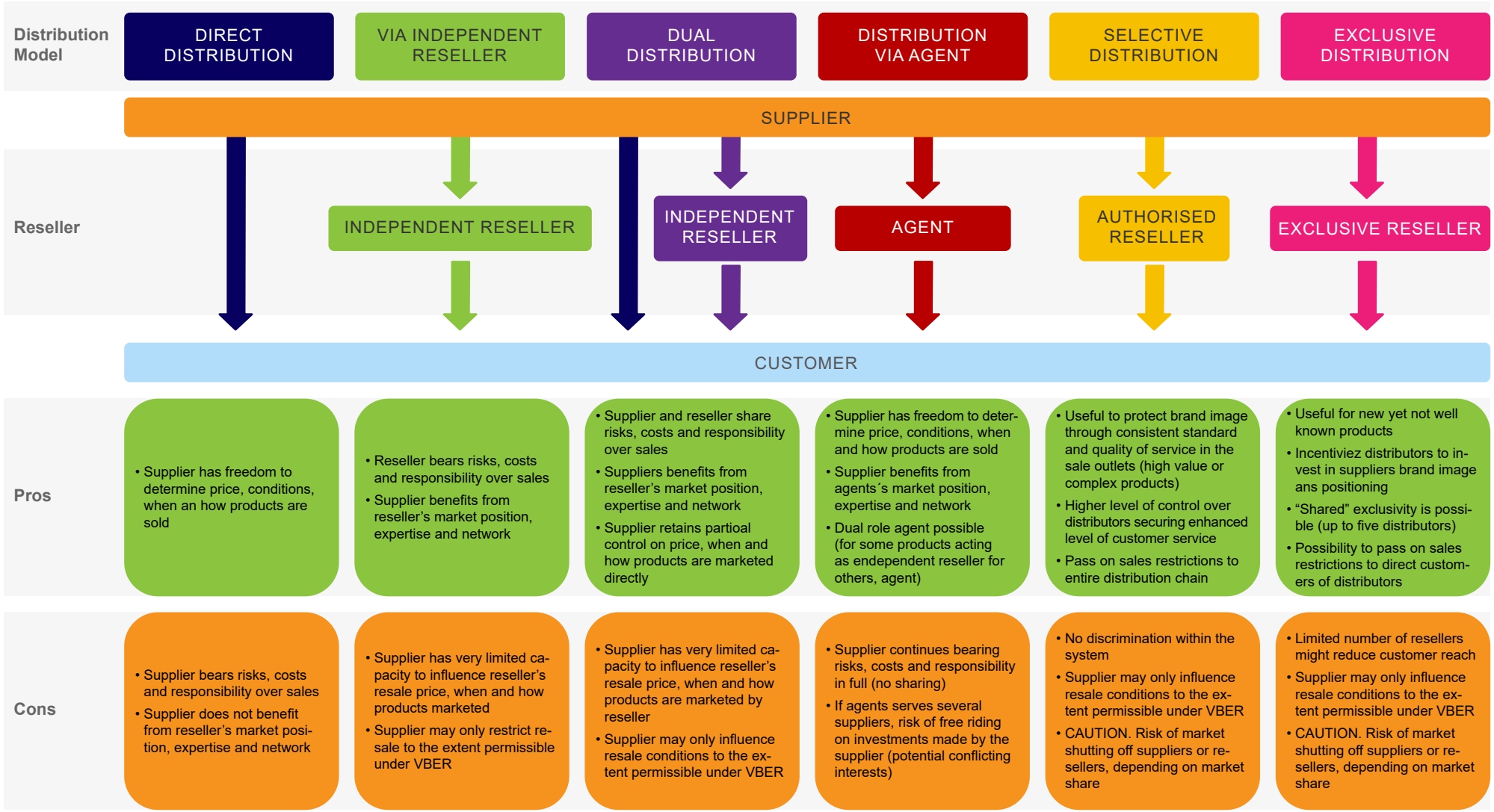
**Could C ask its distributors not to sell on eBay, amazon or any other marketplace and to refrain from using C's brand in search engine advertising?**

No, as this would be considered a strategy to ban marketplace sales and in fact online sales altogether.

* Or any other marketplace, this is just used as an illustrative example.

# D. Distribution models

## I. Overview



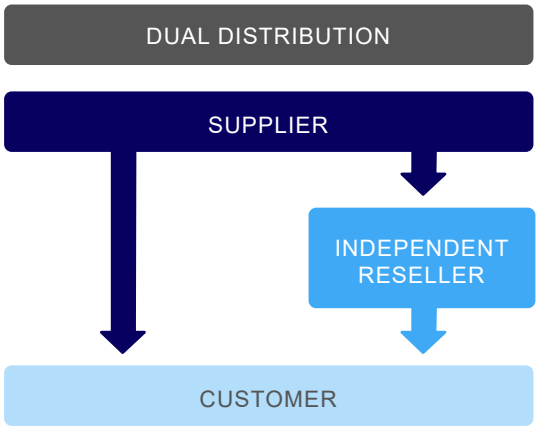
## II. Dual distribution

**Dual distribution** = supplier sells not only through independent resellers but also directly to customers via its own webshop or brick-and-mortar stores

Supplier (= manufacturer or wholesaler or importer) is also retailer who competes downstream with reseller (but reseller does not compete upstream with supplier)

Supplier may enter into non-reciprocal distribution agreements with independent resellers as long as this does not facilitate coordination at retail level

- Be especially careful when exchanging commercial information (see table below for detailed guidance).



## What information can be exchanged between supplier and reseller

(CAUTION: It makes no difference whether information is shared unilaterally [=unrequested] or reciprocally)

### Admissible

- Technical information required to comply with regulatory measures or to adapt products to requirements of customer (e.g., registration, certification, handling, use, maintenance, repair, upgrading or recycling)
- Logistical information (e.g. production processes, inventory, stocks)
- Customer preferences and customer feedback **unless it is used to restrict sales territory**
- Prices charged by supplier and distributor, including information on supplier's RRP or maximum resale prices, if such exchange does not constitute or contribute to a *de facto* RPM practice (i.e. enforce fixed or minimum sale price)
- Promotional campaigns and information on new goods or services
- Performance-related information, including aggregated information relating to marketing and sales activities, if the way such information is disclosed does enable the informed distributor(s) to identify important competitive features (e.g. volume and price) of competing resellers

### Not admissible

- Future prices at which supplier or reseller intend to sell
- Customer specific sales data, unless the exchange of such information is necessary
  - to enable supplier or distributor to satisfy certain specific requirements, e.g. to adapt customised product to end customer's needs, to grant special conditions under loyalty schemes or to provide pre- or after-sales services (guarantee services)
  - to implement or monitor compliance with a selective distribution or exclusive distribution agreement when particular customers were (legally) allocated to the distributor or to the supplier

## Keep in mind

- The lists are only examples, not exhaustive!
- No safe harbours for information exchanges between competitors at same level of trade (e.g. retail or wholesale), so ensure that information provided by reseller does not flow to supplier's direct sales team downstream
- Agreements between supplier/reseller and e-commerce platforms with hybrid function (i.e. platform operator also sells its own products on the platform) do not benefit from any exemption, so even more caution with information exchanges: restrict to minimum necessary.
- It will often remain unclear what is permissible. Take precautions to minimise risks of anticompetitive behaviour, e.g.
  - exchange information only in aggregated form
  - restrict exchange to "old data", i.e. ensure appropriate delay between the time information is generated and exchanging it (3 months to 1 year depending on when information loses its competitive sensitivity)
  - Suppliers: use firewalls, clean teams or other technical / administrative measures to ensure that information communicated by reseller is accessible only to personnel responsible for the supplier's upstream activities on need to know basis

## Hypothetical case

**X has a specialised musical instruments e-commerce platform. Within the platform business, X is both a reseller of musical instruments and he also provides intermediation services to suppliers/resellers, who can sell directly to end-customers through the platform.**

**Can C market its products on X´s platform since C is a competitor of X downstream at retail level?**

Yes, C can sell over the platform but must be cautious because it is hybrid, i.e.

- provides online intermediation services to C and
- competes with C in the sales of clarinets to end-customers.

Because C and X compete at retail level, C must not share commercially sensitive information to avoid any risk of concerted practice. C should reduce information exchange to what is absolutely necessary to enable the sale of C´s clarinets in X`s platform. As precaution, C should require (preferably in contract) that any commercially sensitive information provided to X´s platform business does not flow to X´s downstream retail business unit (e.g. ensure proper firewalls are set and that the intermediation services business unit has staff that does not engage with retail business unit).

In addition, C must monitor the platform's market share: As long as the platform's market share is well below 30% in the sale of clarinets, there should not be any general concerns. Once X becomes a significant market player (>30% share), the assessment should be revised.

**X also resells C's clarinets at retail level.**

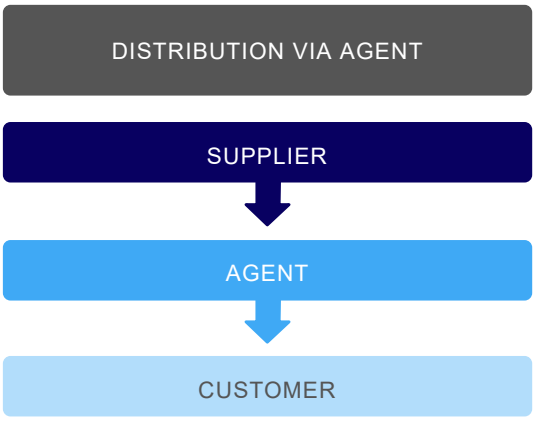
**Can C ask X to provide weekly detailed sales statistics including resale prices at which C's clarinets were sold in order to improve C's own sales strategies?**

No, C and X are competitors at retail level so there should be no information exchange regarding X's current pricing strategy as this is likely to reduce intra-brand competition (= competition between resellers of the same brand) and increase risk of collusion. Weekly reports are up do date commercially sensitive information, so it would generally not be exempted (subject to fines!).

However, providing certain sales statistics could be acceptable if limited to the minimum necessary to enable the implementation of the distribution contract and if necessary to improve the production / distribution of the clarinets, as long as X discloses data that is (i) old (at least 3 months between sale is made and data is shared), and/or (ii) aggregated and (iii) shared only on a need to know basis.

## III. Distribution via Agent

**Agent**
= legal or natural person with power to negotiate and conclude contracts for purchase / sale of goods on behalf of supplier; agent acts as supplier's "long arm", forming one economic unity.




Agent bears no significant financial or commercial risk directly or indirectly related to contracts concluded on behalf of supplier (incl. all investments related to agency agreement),
i.e.

(i) risks directly resulting from contracts concluded/brokered on behalf of supplier (contract-specific risks, e.g. financing and stocks)

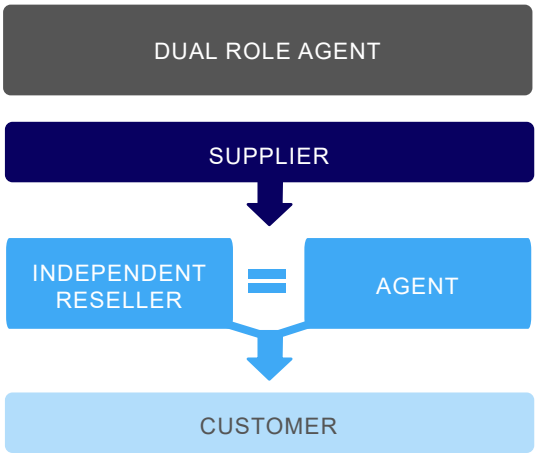
(ii) market-specific investments related to type of activity agent is engaged for (e.g. equipment, software, premises, training, advertising)

(iii) other activities considered necessary by supplier within same product market

Supplier can direct all of agent's activities relating to distribution of its products, e.g.

- set retail price
- identify target customers
- determine advertising strategy, including MAP

**Dual role agent**
= independent reseller for certain products P(1) provided by supplier but also acts as agent for other products P(2) provided by same supplier




To qualify as genuine agent for P(1), reseller must be genuinely free to conclude agency contract concerning these specific goods, for which it bears no financial or business risks (see above).

Supplier can only direct activities, incl. resale prices, for products P(1), where reseller acts as "genuine agent".

## "Genuine" agent

- Does not acquire property in products sold under agency contract
- Does not share costs incurred in supplying, providing or acquiring goods or services, incl. transportation costs
- Does not store goods at own expense or risk
- Does not take responsibility in case of customer defaults, unless agent is at fault (e.g. non-compliance with security or anti-theft measures)
- Does not assume responsibility towards customers or third parties for losses or damages arising from supply of goods or services, unless agent is at fault
- Has no obligation to invest in sales promotions, unless fully reimbursed by supplier
- Incurs no market-specific investments, unless fully reimbursed by supplier
- Does not assume other activities for supplier within same product market but beyond scope of agency agreement (e.g. delivery), unless fully reimbursed by the supplier

## Borderline cases: Seek advice!

- "Agent" acquires ownership of supplier's products for short period of time but does not bear any costs or risks in connection with transfer of ownership
- "Agent" carries out transport services, but costs are covered by supplier
- "Agent" contracts with large number of suppliers
- "Agent" is traditionally an independent reseller but assuming "agency" for several suppliers through "shop in shop" models
- **Agency contract with online platform operator** will generally not qualify as genuine agency agreement where:

  (i) platform operator serves large number of suppliers,

  (ii) platform operator (rather than supplier) determines conditions and commercial sales strategy (imbalance in bargaining power),

  (iii) platform operator makes significant market-specific investments (e.g. software, advertising and after-sales services), bearing financial or commercial risks associated with the intermediated transactions.

## Keep in mind

- Misuse of agency concept can lead to hardcore restriction (subject to fines!), e.g. where supplier does not actually take all associated distribution decisions and does not assume all related risks, but rather establishes an easy way to control retail prices for those products that allow high resale margins.
- Specifically in a dual agent scenario, retailer must be able to prove that agency criteria are met.
  - CAUTION where agent plays dual role **for same range of products:** It may be hard to single out investments and costs related to agency function from those relating solely to independent reseller function!
  - Keep record of all relevant documentation (in writing).
- **Multi-brand agent,** i.e. several suppliers using same agent because they might decide to collectively exclude other suppliers from using that agent, or use agent to collude and/or exchange commercially sensitive market information (reducing competition between brands)
  - CAUTION where suppliers with combined market share >30-50% use same agent

## Hypothetical case

**C intends to release a high-end clarinet combining new technological features and sophisticated design. To make sure the new product is appropriately marketed and potential buyers have high quality customer service, C wants to establish an agency agreement with one of its best-performing independent resellers: Premium distributor P, who resells musical instruments for many brands.**

**Can C, through an agency agreement, retain control of all marketing features of the premium clarinet, such as (i) pricing, (ii) locations where clarinets will be sold, (iii) customer group to which marketing strategy should be addressed, and (iv) display of the clarinets in the stores?**

P would, in such case, become a dual role agent because P also sells clarinets for C as an independent reseller as well as other musical instruments. C must make sure that with respect to C's different clarinets, P's roles are clearly defined and separated.

- C must keep well documented proof that all the investments and risks related to the distribution of the new product line are incurred by C and not by P.
- C should provide dedicated sales personnel acting specifically for the sale/marketing/advice of the high-end clarinet in P's store.
- P should keep separate account of the revenues generated with the high-end clarinet as opposed to the other products and ideally have a separate cashier.
- It should be obvious to the customer in terms of marketing material, sales display etc that P assumes a different role with respect to the high-end clarinet than his role as independent reseller for the other products ("shop in shop").
- Where it is difficult to single out which of P's investment specifically relate to the new product line, C should cover all of P's market-specific investments to distribute C´s clarinets (new product line and other clarinets), e.g. equipment, premises, training, and advertising. A pro-rata approach would not be acceptable, since it is difficult to single out which investments benefit exclusively the new product line.

## Hypothetical case

**Can C require that P does not act as agent and/or distributor for other brands that compete with C (single branding provision)?**

C could potentially require single branding if C has legitimate reasons to fear that competing brands would free ride on its investments (e.g. pre-sales personnel training, logistics investments) made in the agency agreement or could have access to commercially sensitive information (e.g. strategic and transfer of relevant non-public know-how). However, the answer is not clear-cut. It depends on a case-by-case analysis taking into account, e.g.

- P's market shares and whether there would be a risk that distribution channels are shut off to other clarinet suppliers (especially where P has market shares close to/ over 30% of the sales force for clarinets),
- whether other clarinet or musical instrument producers also have similar arrangements in place (combination of effects)? If more than 40% of total sales force are covered by similar single branding agreements, this could hinder distribution channels available to competing suppliers. However, small suppliers with a market share at/below 5% are generally not considered to contribute significantly to a combination of effects.

**P already serves as agent for more than two musical instrument suppliers: flutes for F and guitars for G. Can C still enter into an agency agreement with P for the sales of clarinets?**

There is no clear restriction. Generally, an agent can act for more than one supplier in different product markets. However, the more principals the agent serves, the harder it will be to satisfy the "genuine agent criteria" because P might end up making significant market-specific investments that benefit all three suppliers, i.e. general marketing campaigns, sales personnel, administrative costs, cashiers.

In order to be able to prove that P is acting as a genuine agent with respect to the clarinets (as well as the flutes and guitars), P`s costs should be clearly defined to fulfil each agency contract separately, that is:

C should bear all costs relating to the sales of its products and to promoting the sales of C's clarinets (e.g. furnish P`s shops in order to display and sell C's products, costs for storage equipment, provide dedicated sales personnel acting specifically for the sale/ marketing/advice of C clarinets), P should keep separate account of the revenues generated with C clarinets as opposed to other products and ideally have a separate cashier and it should be obvious to the customer in terms of marketing material, sales display etc that P assumes an agency role with respect to C clarinets ("shop in shop").

The same applies to F's flutes and G's guitars, respectively.

## Hypothetical case

**P already serves as agent to other clarinet suppliers. If C enters into an agency agreement with P, would it be able to benefit from a safe harbour?**

Even if P acts as a genuine agent, the answer is not clear-cut because competitors use the same agent. If all suppliers using the same agent represent (altogether) >50% of the market for the supply of clarinets, no safe harbour applies; assessment to be made on whether such agreement is likely to facilitate collusion, i.e. suppliers are likely to

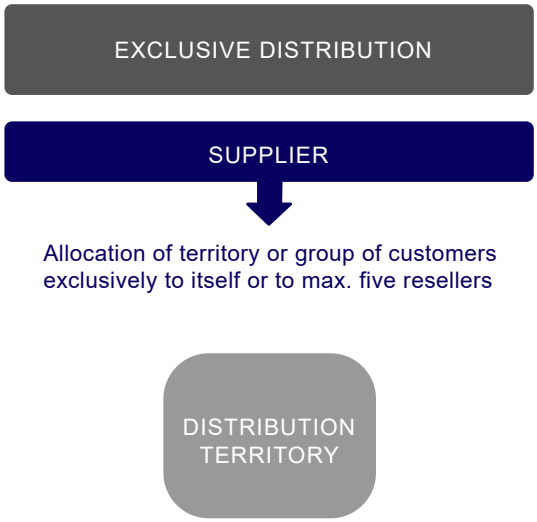
- collectively exclude other suppliers from using those agents,
- collude on market strategy,
- exchange sensitive market information.

## IV. Exclusive Distribution

**Exclusive distribution**
= supplier allocates territory or customer group exclusively to itself or to one or more reseller (i.e. supplier restricts all other resellers from selling into this territory or to this customer group)

Can be admissible where:

- no restriction of passive sales, i.e. non-exclusive resellers remain free to respond to unsolicited requests
- market share < 30%
- where market shares > 30%: careful assessment required (Duration should be limited to max. 5 years)




**Active vs. Passive Sales**
“Active sales” = actively targeting customers

- An online sales operator is considered to actively sell to /target a territory outside its designated area whenever it (i) offers language options on websites other than those used in the designated territory, (ii) offers a website with a domain name corresponding to that of the targeted territory, (iii) carries out advertising and promotional campaigns outside its designated territory.

“Passive sales” = responding to unsolicited requests from customers without actively initiating the sale or specifically targeting territories or customer groups

## What's allowed for suppliers?

### Admissible

- Grant exclusivity limited to active sales, i.e. passive sales by non-appointed resellers are still possible in the territory/to the customer group
- Appoint up to five exclusive resellers for one territory or a particular group of customers
- Restrict active sales to territories or customer groups exclusively allocated to other resellers or reserved for itself
- "Roll over" such restriction to the reseller's direct customers, i.e. require reseller to pass it on
- Restrict the exclusive reseller's place of establishment (i.e. location clause)
- Restrict active or passive sales by exclusive wholesaler to end consumers
- Restrict sales of components to customers who could use them to manufacture goods that compete with supplier
- Require reseller not to buy, sell or incorporate competing goods (single branding). If non-compete is agreed for >5 years, reseller should be able to terminate contract (at reasonable cost and notice period)

### Borderline cases: Seek advice!

- Restrict the territory or customer group the selected resellers may sell the goods to is only exempted if one of the situations indicated in the green column applies

### Not admissible

- Appoint exclusive distributor for all sales in the territory / to the customer group (including passive sales)
- Restrict cross-supplies between exclusive distributors
- Restrict participation in public and non-public tenders
- Restrict active or passive sales by reseller´s indirect customers
- Restrict **passive** sales into a territory or to a customer group exclusively allocated to other distributor(s) or reserved for itself

## Keep in mind

1. "Safe harbour" only applies where market share of both supplier and reseller is <30%. Where market shares are >30%, supplier will need to prove that an individual exemption applies (burden of proof! keep record of relevant documentation), specifically why exclusivity is important to protect the brand image or assure proper use of the product.
2. Where many suppliers with combined market share >50% use exclusive and/or selective distribution systems, competition concerns may arise due to a combination of effects:
   - where suppliers use the same exclusive/authorised distributor (multi brand distributor): increased risk of collusion and reducing competition between brands
   - where suppliers combine exclusive/selective distribution with single branding (=only supplier's products may be sold): risk of shutting off potential suppliers from finding alternative resellers and of reducing competition between brands, at least where agreements apply to a significant number of resellers (>40% of market).
3. Where supplier operates a selective distribution system, special rules apply (next section).

## Hypothetical case

**In country Y, where C has a very moderate market share (well below 15%), C considers adopting an exclusive distribution system to incentivise distributors to invest in promoting C's products and improve its brand image. Can C appoint distributors D1 and D2 exclusively for the territory of Y?**

Yes, C can appoint exclusive resellers (up to 5) provided C does not restrict the ability of other distributors to respond to unsolicited inquiries from Y ("passive sales").

**Can C require D1 and D2 to distribute only C clarinets to assure they concentrate their efforts in marketing C´s good, i.e. not to include in their portfolio clarinets from other brands?**

Yes, including a single branding obligation on the reseller would be admissible since C's market share is well below the 30% threshold. In addition, it is particularly defensible when aimed to preserve C's brand image, assuring that resellers focus on specialised sales force training, special display and product enhancing events for C's products. This is particularly the case when C makes investments in the promotion of its products at the resellers premises and on the relationship with the reseller (e.g training and know how transfer) and wants to avoid free-riding by competitors.

Be aware that if a non-compete obligation exceeds five years, the reseller should be able to renegotiate or terminate the agreement by giving a reasonable period of notice and at a reasonable cost.

Also worth noting that if many other suppliers adopt parallel networks of single-branding arrangements and altogether exceed 40% sales force coverage, this may raise competition concerns of limiting distribution options to other suppliers and of reducing inter-brand competition. A market share of less than 5% is generally not considered to contribute significantly to such a cumulative effect.

**Distributor D is exclusive distributor for two clarinet suppliers in country Y (exclusive multi brand distributor. Can C also enter into an exclusive agreement with D?**

Yes, provided that the combined market share of the brands distributed by D is not >30%. The higher the combined market share of the suppliers working with the same exclusive distributor, the higher the concerns of collusion and that this might restrict competition between the competing brands.

## Hypothetical case

**Can C protect the investments made by D1 and D2 by prohibiting sales into country Y by distributors active in other EU-countries?**

Yes, C can prevent active sales into country Y by resellers active in other countries provided it does not prohibit passive sales. Online sales are generally considered passive sales, however webshop operators would be considered to be actively selling in Y (i) if they adapt the domain name or language options to better address the customers in that country (e.g. offers languages that are not commonly used in the territory where the resellers is established), or(ii) if carry direct advertising and promotional campaigns (including price comparison services or advertising on search engines) in Y.

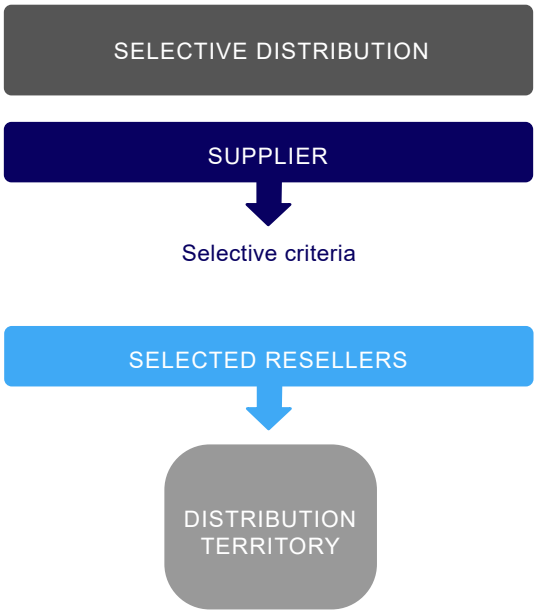
**Can C require from D1 and D2 that they do not sell to each other?**

No, restricting cross supply among two exclusive resellers would not be acceptable because it restricts the supply sources of the distributors and therefore limits intra-brand competition (=competition between resellers of the same brand).

## V. Selective Distribution

**Selective distribution system**
= supplier sells products only to re-sellers selected on the basis of specified criteria

The selected reseller(s) are protected against active and passive sales by unauthorised resellers.




**Quantitative vs. qualitative distribution system**

Quantitative criteria limit the number of resellers directly by, for instance, imposing a fixed number of resellers.

Qualitative criteria limit the number of resellers indirectly, by imposing conditions that cannot be met by all resellers, for instance, relating to the product range to be sold, the training of sales personnel, the service to be provided at the point of sale or the advertising and presentation of the products.

The supplier is not obliged to publish its selection criteria.

**Open vs. closed selective distribution system**

In “open” selective distribution systems, neither supplier nor reseller are subject to contractual restrictions on the sale of the contract products. The supplier can, however, oblige reseller to comply with certain qualitative requirements.

In a “closed” selective distribution system, resellers must not sell the goods received from the supplier to unauthorised resellers within the territory reserved by the supplier to operate that system.

## What's allowed for suppliers?

### Admissible

- Qualitative selective distribution system is admitted provided the following three criteria are met:

  (i) nature of the goods or services requires a selective distribution system, e.g. high-quality or technically complex product

  (ii) resellers must be chosen on the basis of objective qualitative criteria, which are laid down uniformly for all potential resellers and are not applied in a discriminatory manner (different criteria may be set for online and offline channels)

  (iii) criteria does not go beyond what is necessary

- Quantitative selective distribution system is admitted provided not more than 5 selected resellers

- Restrict active or passive sales to unauthorised distributors located in a territory where supplier operates a selective distribution system
- "Roll over" such restriction to entire distribution chain, i.e. require reseller to pass it on
- Restrict the place of establishment of the selected distributor (i.e. location clause)
- Restrict active and passive sales by authorised wholesaler to end consumers
- Restrict sales of components to customers who could use them to manufacture goods that compete with supplier
- Require reseller not to buy, sell or incorporate competing goods (single branding). If non-compete is agreed for >5 years, reseller should be able to terminate contract (at reasonable cost and notice period)

### Borderline cases: Seek advice!

- Restrict territory or customer group which selected distributors may sell goods to is only exempted if one of the situations indicated in the green column applies
- The restriction of active sales to end users by members of selective distribution system operating at the retail level of trade is exempted if (i) such territory or customer group is exclusively allocated to other distributor(s) or (ii) the sales are made outside the authorised place of establishment

### Not admissible

- Restrict cross-supplies between selected distributors operating at same or different levels of trade (e.g. wholesale and retail)
- Restrict participation in public and non-public tenders
- Restrict passive sales to end consumers by an authorised distributor operating at the retail level

## Keep in mind

1. "Safe harbour" only applies where market share of both supplier and reseller is <30%. Where market shares are >30%, supplier will need to prove that individual exemption applies (burden of proof! keep record of relevant documentation), specifically the importance of selected resellers to protect supplier's brand image and/or assure proper use of the products sold.
2. Where many suppliers with combined market share >50% use exclusive and/or selective distribution systems, competition concerns may arise due to a combination of effects:
   - where suppliers use the same exclusive/authorised distributor (multi brand distributor): increased risk of collusion and reducing competition between brands
   - where suppliers combine exclusive/selective distribution with single branding (=only supplier's products may be sold): risk of shutting off potential suppliers from finding alternative distributors and of reducing competition between brands, at least where agreements apply to a significant number of resellers (>40% of market)

## Hypothetical case

**In country W, where C has a very moderate market share (well below 15%), C intends to adopt a selective distribution system to assure that its resellers meet certain standards or quality of service in its outlets.**

**Can C select its resellers based on such "quality criteria"?**

Yes, since C's market share is below 30%, C can benefit from an exemption if resellers also have market shares below 30%. C wants to make sure that resellers aim to preserve the brand image of C's clarinets through specifically-adapted marketing features and high-quality of customer service, which should be reflected in the criteria C applies to select resellers, e.g. they must sell a certain product range, train their sales personnel, provide a certain standard of service at the point of sale, display products in a certain way etc. These criteria must be applied equally to all potential resellers, not in a discriminatory manner.

**Can C require different qualitative criteria for online/offline sales?**

Yes, C can impose different criteria to address different requirements for online and offline stores. For instance, C could require online resellers to set up after-sales helpdesk or to cover customers' costs of returning purchased products.

**Is C's selective distribution system still admissible when other clarinet suppliers also adopt selective or exclusive distribution systems?**

Where selective or exclusive distribution systems are implemented by many suppliers, if such arrangements cover more than 50% of the market for the supply of clarinets, the cumulative effect may prevent a category of resellers (e.g. discounters) from having supply options, which could affect intra-brand competition (=competition between resellers of the same brand). A market share of less than 5% is generally not considered to contribute significantly to such a cumulative effect.

**Can C require selected resellers to sell exclusively C clarinets to assure they concentrate their efforts in marketing C´s goods, i.e. not to include in their portfolio clarinets from other brands?**

Yes, including a single branding obligation (=only supplier's products may be sold) would be admissible since C's market share is well below the 30% threshold. In addition, it is particularly defensible if aimed to preserve C's brand image.

If many other suppliers adopt parallel networks of single-branding type arrangements and altogether exceed 50% of the sales force for clarinets, this may raise competition concerns of limiting distribution options to competing suppliers and of reducing inter-brand competition. A market share of less than 5% is generally not considered to contribute significantly to such a cumulative effect.

**C operates a selective distribution system in countries Y and Z. Can C restrict sales from authorised reseller in Y from selling to authorised reseller in Z?**

No, if countries Y and Z are within supplier's EEA selective distribution system, this would restrict cross-supplies and be considered a hardcore restriction (subject to fines!). C may impose restrictions under exceptional circumstances but should seek legal advice so that the specific circumstances can be assessed.

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