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The European Commission issues helpful draft guidance on information exchange in a dual distribution context

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On 4 February 2022, the European Commission ("Commission") published (for a brief period of public consultation) revised draft guidance on dual distribution, available here, which includes an extensive discussion concerning information exchange (the "Draft Guidance"). This is likely to be one of the final steps in the lengthy process towards the replacement of the current Vertical Agreements Block Exemption (Regulation (EU) No 330/2010 ("VBER")) and the Guidelines on Vertical Restraints ("VGL"). The Draft Guidance fills an important gap left by the drafts of both the new VBER and the new VGL released by the Commission on 9 July 2021, which, whilst to a large extent excluding information exchange conducted in the context of dual distribution from the benefit of the draft new VBER, provided no specific guidance on how the compatibility of such information exchange with Article 101 Treaty on the Functioning of the European Union ("TFEU") would be assessed (see VBB on Competition Law, Volume 2021, No. 7). Furthermore, the Draft Guidance indicates that the scope of the exclusion of such information exchange from the safe harbour of the VBER will be reduced compared to what was suggested by the draft new VBER. Both this softening of approach and the new extensive practical guidance are to be welcomed. For the most part, the proposed new rules should enable suppliers to collect the data they need to obtain an enhanced understanding of the nature of demand for their products, and thereby improve both the distribution of their products and their competitiveness against other brands.

Below, we summarise the rules applicable to dual distribution both under the current VBER and under the July 2021 draft texts of the new VBER and VGL, before describing the contents of the Draft Guidance in particular concerning information exchange.

1. CURRENT RULES

Dual distribution refers to a scenario where a supplier sells goods (or services) to an independent distributor in a vertical relationship, but also competes downstream with the distributor by selling those goods (or services) through, for example, the supplier's own stores. Under the rules currently applicable to dual distribution, by virtue of Article 2(4) VBER, non-reciprocal agreements fall under the block exemption without any limitations provided that the buyer of the supplier's goods (i.e., the distributor) is not also a manufacturer of competing goods. It has generally been understood that the block exemption also applies to vertical information exchanges between the supplier and the distributor, with the likely limited exception of certain exchanges which amount to horizontal collusion (see VBB on Competition Law, Volume 2020, No. 7). The accepted rationale for this approach has been that, in a dual distribution context, the vertical agreement's potential negative impact on the competitive relationship between the supplier and buyer at the downstream distribution level is generally considered to be less important than the vertical agreement's potential positive impact on competition in both the supply and distribution of the supplier's goods (where they compete with the goods of other manufacturers).

2. JULY 2021 DRAFT VBER & VGL

In a marked change of approach, the Commission introduced several limitations to the existing exemption in the July 2021 drafts of the new VBER and VGL. The Commission justified these changes by referring to the substantial increase in the prevalence of dual distribution, resulting

from the growth of online sales, which have facilitated larger-scale direct sales by suppliers, either through their own web-shops or via online marketplaces. Fearing that the current rules for dual distribution, in particular in relation to information exchange, could lead to many vertical agreements with possible serious horizontal concerns being exempted, the Commission proposed that information exchange in dual distribution systems would only be block exempted if, among other conditions, the parties' combined retail market share did not exceed 10%. Where the parties' aggregate market share at retail level would exceed 10% but their individual shares would not exceed 30% in the relevant sale and purchase markets, the block exemption would apply to (non-reciprocal) vertical agreements concluded between the parties (i.e., distribution agreements), but not to exchanges of information between the parties. Finally, regardless of market share, any vertical agreement in a dual distribution system would be excluded from the safe harbour provided by the block exemption if it was considered to restrict competition by object, including by way of information exchange.

This restrictive proposal was heavily criticised in the consequent public consultation (see also VBB Insights, 9 August 2021, The Commission's Draft VBER and VGL – Key Changes). It was clear that these proposed rules risked materially affecting suppliers operating dual distribution systems, especially because any successful and effective – vertical – relationship between a supplier and its retailers will almost invariably require the sharing of information about sales, products, marketing campaigns, market trends, and consumer preferences on a continuous basis. Under these proposed rules, as soon as the parties' market share would exceed 10%, all sharing of information would no longer benefit from the block exemption, and, furthermore, information sharing would be excluded from the block exemption altogether, regardless of market share, if it was considered to amount to a restriction by object. The unsatisfactory nature of these proposals was compounded by the fact that no guidance was given on what type of information exchanges in a vertical relationship might still be permitted, which – the Commission had suggested – would be provided later in the new Horizontal Guidelines (itself an inappropriate context for such advice given that dual distribution agreements are fundamentally vertical agreements).

3. NEW DRAFT GUIDANCE

In light of this valid criticism, the Commission has now modified its proposed approach as reflected in the Draft Guidance. First, the Commission moves away from the specific market share-based approach described above: the application of the block exemption to information exchange in the context of dual distribution would no longer depend on the parties' market share on the retail market, and the only market share threshold would be the 30% threshold applicable to the parties' individual positions in, respectively, the sale and purchase markets (Article 3 VBER).

Second, whether the exchange of information between the parties would be covered by the block exemption would (exclusively) depend on whether it is considered "necessary to improve the production or distribution of the contract goods or services by the parties" (wording to be included in the new Article 2(5) VBER). Information exchange that would not satisfy this test (though not the distribution agreement in the context of which it was exchanged) would be excluded from the benefit of the block exemption and would need to be assessed under Article 101 of the Treaty on the Functioning of the European Union ("TFEU"), taking into account the Horizontal Guidelines and the relevant case law of the Court of Justice of the European Union ("CJEU") relating to exchanges of information between competitors. In this respect, it is noteworthy that the draft new Horizontal Guidelines published by the Commission for consultation on 1 March 2022 (the "Draft Horizontal Guidelines") do not provide any specific guidance in relation to information exchange in the context of dual distribution falling outside the scope of the VBER.

Third, the new draft provides fairly detailed guidance as to what constitutes information "necessary to improve the production or distribution of the contract goods or services by the parties" and thereby would benefit from the block exemption. From a practical perspective, the most valuable part of the Draft Guidance comprises the two "non-exhaustive" lists of: (i) information the exchange of which would generally be able (subject to certain exceptions) to benefit from the exemption; and conversely (ii) information the exchange of which would generally not be block exempted.

Information the exchange of which would generally be considered to meet the requirements of the block exemption, whether (generally) provided by the buyer or by the supplier, includes the following (whether the information concerns past, current or, except where expressly stated otherwise, future conduct):

i. Technical information, for example related to the registration or certification of the contract goods or services;

ii. Information relating to the supply of the contract goods or services, including relating to production, inventory/stock, sales volumes and returns;

iii. Aggregated information relating to customer purchases of the contract goods or services, customer preferences and customer feedback (in contrast, as explained below, customer-specific information would not generally be viewed favourably);

iv. Information relating to the prices at which the contract goods or services are sold by the supplier to the buyer;

v. Information relating to the supplier's recommended resale prices or maximum resale prices for the contract goods or services, and information relating to the prices at which the buyer resells the goods or services (excluding, generally, information on future "downstream" sale prices, as well as the use by the supplier of the buyer's information for the purpose of retail price fixing);

vi. Information relating to the marketing of the contract goods or services, including information on new goods or services to be purchased and sold under the vertical agreement, as well as information on promotional campaigns for the contract goods or services; and

vii. Performance-related information, including:

    a. aggregated information communicated by the supplier to the buyer relating to the marketing and sales activities of other buyers of the contract goods or services (which must not enable the buyer to identify activities of competing buyers); and

    b. information regarding the volume or value of the buyer's sales of the contract goods compared to its sales of competing goods.

In contrast, the exchange of the following types of information would generally be excluded from the safe harbour:

i. Information relating to the actual future prices at which the supplier or buyer would sell the contract goods or services downstream (unless necessary to organise the type of coordinated short-term low price campaign viewed favourably according to the section of the draft VGL concerning resale price maintenance);

ii. Customer-specific sales data, including non-aggregated information on the value and volume of sales per customer, or information that identifies particular customers (unless necessary to enable the adaption of contract goods/services to the consumers' requirements or to provide guarantee or after-sales services, or to allocate customers under an exclusive distribution agreement); and

iii. The exchange of information relating to goods sold by a buyer under its own brand name where the supplier to which it provides the information is a manufacturer of competing branded goods, unless the manufacturer is also the producer of the own-brand goods. (As a separate but related point, it should be noted that where such 'private label' goods are produced by a retailer, rather than out-sourced, the block exemption would not apply at all to agreements concluded by the retailer with suppliers in a dual distribution context. This questionable exclusion (taking into account that even major 'manufacturer' brands often do not own manufacturing facilities) would not be limited to information exchange engaged in by the retailer with such suppliers but also to the overall distribution relationship.)

The Commission refers to several precautions which parties can take to minimise the risk that the information exchange could raise horizontal concerns in the event that it does not benefit from the block exemption for the type of reasons described above. These include limiting the exchange to aggregated sales information or using an appropriate delay between the generation of the information and the exchange (draft revised guidance on these concepts – which does not make reference to dual distribution – being included in the Commission's Draft Horizontal Guidelines). A further precaution would be the use of administrative or technical measures, such as firewalls, that ensure that information provided by the buyer is only available to the personnel of the supplier responsible for its upstream activities (i.e., its relations with independent distributors) and not personnel responsible for the supplier's downstream direct sales activity (e.g., its own retail business).

4. COMMENTARY

In conclusion, the Draft Guidance represents an encouraging development for companies active in dual distribution. Although the applicability of the block exemption to information exchanges would depend on an abstract and potentially demanding test being met (which, by requiring such an exchange to be "necessary" for the "improvement of production or distribution of goods", does no more than specify that two of the main conditions of Article 101(3) TFEU should be met), the guidance itself makes clear that at least most of the information that a supplier and a distributor would wish to exchange to ensure the efficient distribution of the supplier's products will be treated as meeting this test. It is reassuring that distributors would be able to provide suppliers with granular and real-time information on sales volumes, stock levels, marketing strategies and prices of the supplier's products (with the exception of future prices), as well as comparative data on competing products and distributors for benchmarking purposes (without being subject to the constraints of internal firewalls). There would, however, seem to be no sound competition law justification for viewing negatively the exchange of customer-specific sales and price data provided, of course, that applicable data protection rules are complied with. Indeed, it is unclear why mere awareness of such information would be assumed likely to lead to a substantial restriction of competition when misuse of such information to prevent sales by distributors to specific customers would itself be a clear hardcore restriction (bar in clearly defined exceptional circumstances), a rationale which seems to have rightly persuaded the Commission not to negatively view the exchange of granular sales and price data.

It is regrettable that no specific guidance is provided for situations where the benefit of the block exemption is not available for reasons of market share (rather than because of the type of information that is exchanged). This is unfortunate as the exchange of some of the information viewed positively by the Draft Guidance (in respect of future intentions) might be considered to amount to a restriction by object under the standards of the Draft Horizontal Guidelines unless the specific context of dual distribution is recognised to justify a more nuanced approach.

The fact that only the Commission – and not the national competition authorities or the EU or national courts – would be bound by the Draft Guidance (in contrast to the provisions of the block exemption itself which bind *erga omnes*) could be a concern, and it can only be hoped that the Commission's approach will be followed by these bodies to ensure both an effective and a consistent competition policy across the EU.

The next, and final, development in the Commission's lengthy review of the VBER is expected to be the adoption of the new VBER and VGL, which will then enter into force on 1 June 2022. The new Horizontal Guidelines should be finalised so as to take effect on 1 January 2023.

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