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European Commission's E-Commerce Sector Inquiry Leaves Unanswered Questions on Enforcement

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The European Commission's Preliminary Report on its sector inquiry into competition in e-commerce was published on 15 September. Although the Preliminary Report only sets out the Commission's initial findings, these are unlikely to change materially between now and the final report, which is due to be published by the end of the first quarter of next year. The Preliminary Report therefore serves as a useful guide on the Commission's thinking on a number of key issues and indicates those areas with which it has the most serious concerns. The rather inconclusive nature of the document, which is largely taken up with statistical descriptions of various aspects features of European e-commerce, means that many key questions remain unanswered, however. In particular, there is no clear indication yet of what the Commission's findings mean for future enforcement action.

Background

The stated aim of the e-commerce sector inquiry, which was launched in May 2015 as part of the Commission's wider Digital Single Market strategy, was to enable the Commission to gain a better understanding of the functioning of e-commerce markets within the EU and to identify existing and emerging restrictions of competition that could infringe EU law. The underlying motivation was the Commission's wish to promote cross-border e-commerce in Europe, as a manifestation of its overriding policy goal of creating a meaningful single market across the EU that provides visible benefits to consumers.

Within the broad category of e-commerce, the Commission separated its work into identifying restrictions on the sale of certain consumer goods, on the one hand, and on the provision of digital content, on the other. A wide range of market participants received questionnaires, including retailers, manufacturers, online marketplaces, rights-holders and broadcasters. The resulting inquiry, which produced responses from over 1800 companies and required the disclosure of over 8000 contracts, is the largest the Commission has initiated since it gained the power to undertake sector inquiries in 2004.

Notwithstanding the broad scope of the inquiry, and the effort involved on the part of respondents and the Commission, it is important to note its limitations at the outset. The Commission's powers to undertake sector inquiries do not extend to the ability to impose remedies or change the law. Rather, the Commission is able to use information gathered in the course of a sector inquiry as the basis for enforcement action against specific businesses, under the antitrust provisions of the Treaty on the Functioning of the European Union (TFEU) or to inform wider policy initiatives.

It is notable that the legal framework within which restrictions on online sales are assessed is largely set by Article 101 TFEU, which prohibits anticompetitive agreements, and the Vertical Agreements Block Exemption Regulation (VBER), which exempts vertical supply agreements from Article 101 as long the parties' market shares do not exceed 30% and provided that they do not contain hardcore restrictions of competition. The legal status of common restrictions of the online sale of physical products is extensively considered in the Commission's 2010 Vertical Agreements Guidelines, which attempt (not always successfully) to strike a balance between the often conflicting interests of brands and online retailers. As the VBER and Verticals Guidelines are set to remain in place until their expiry in 2022, the basic legal framework is effectively fixed. (The Commission has nevertheless confirmed that the results of the sector inquiry will feed in to the range of legislative initiatives, beyond the competition law regime, that are being

undertaken in the context of the Digital Single Market strategy.)

The Preliminary Report

Given this context, it is unsurprising that the Preliminary Report is primarily concerned with simply describing various aspects of European e-commerce revealed by the responses to its questionnaires. The legal analysis largely restates the current law, while clarifying the Commission's position on contentious issues that were inadequately addressed by the Vertical Guidelines. There are, at best, some hints as to potential areas for future enforcement action, as the Commission indicates restrictions that in its view raise particular concerns.

Reflecting the structure of the inquiry, the Preliminary Report takes a notably different approach to analysing restrictions on the sale of consumer goods and digital content, with the section dealing with the former containing a far more specific analysis of restrictions and their compatibility with EU competition law. In contrast, the section on digital content distribution is almost entirely descriptive and there is no legal analysis to speak of.

Consumer goods

The Preliminary Report contains a large amount of detail on the prevalence of specific business models and restrictions on online sales across the EU. While it is moderately diverting to note the wide variations in commercial practices across the EU, including for example that selective distribution is more common in France than in the UK or that marketplaces are particularly important for SMEs in Germany, many of the conclusions that the Commission draws from the data gathered are rather vague. For example, the Commission finds that price transparency has both favourable and unfavourable consequences, which does not take the debate very far.

More interesting is the Commission's recognition that customers increasingly switch between online and offline sales channels and that manufacturers appear to be responding to this through increased use of exclusivity and selective distribution systems to restrict online sales. (This development has been described as a "Renaissance of vertical restraints" by the official in charge of the sector inquiry.) Indeed, almost half of the manufacturers using selective distribution who responded to the inquiry reported that they do not allow online operators who have no physical shops to join their selective distribution network. The indication in the Verticals Guidelines that a requirement that members of a selective distribution network must have a physical shop is generally permissible, even though it legitimises the exclusion of 'pure play' online retailers from admission, was the most contentious aspect of the last review of the Vertical Guidelines. The fact that so many brands appear to have taken advantage of this provision in practice may lead to the Commission taking a firmer line on such practices in future.

In a similar vein, the Preliminary Report suggests a subtle hardening of the Commission's position on marketplace sales bans. The last sentence of para 54 of the Verticals Guidelines, which indicates that "where [a] distributor's website is hosted by a third party platform, the supplier may require that customers do not visit the distributor's website through a site carrying the name or logo of the third party platform" has sometimes been used by brands to argue that outright bans on the use of online platforms by retailers are always permitted, without any need for objective justification. While this reading arguably ignores the context for this statement, which concerns potential quality-based justifications for such bans, the wording is certainly ambiguous. The Preliminary Report makes it clear that, while the Commission takes the view that a marketplace sales ban is not a hardcore restriction of competition, such a restriction can be anticompetitive in particular circumstances (i.e. it is not presumptively lawful). It also notes that it will be harder for a brand to justify such a ban in circumstances where it sells on the relevant marketplace itself, in its own name, or if it supplies the marketplace operator within its selective distribution system, since this would imply that the marketplace provides a satisfactory retail environment.

Ultimately, the Commission indicates, a case by case approach is required to assess the legality of marketplace restrictions.

Further clarification of the law is awaited from the Court of Justice of the European Union, which is considering a reference concerning the legality of outright online marketplace sales bans in the *Coty* case.

A similarly nuanced approach is taken to the highly contentious area of parity agreements or most favoured nation clauses. The use of such clauses by online hotel booking sites has recently led to a rash of competition enforcement cases by national authorities and a marked divergence in approach between the German Federal Cartel Office and national courts, on the one hand, and other EU National Competition Authorities on the other. Understandably, the Commission takes an even-handed approach to such clauses, noting that they may dis-incentivise retailers to compete on price and reduce intra-brand competition, while acknowledging that they may lead to efficiencies, help to recoup investments and avoid free-riding. Therefore, again such clauses need case by case analysis, as do restrictions on retailers' ability to use price comparison tools.

A more hard-line approach is taken towards restrictions that clearly fall within the category of hardcore restrictions that are presumed to infringe Article 101 TFEU and thus already fall outside the protective scope of the VBER. These include resale price maintenance, bans on cross-border sales and measures that either prevent online sales or discriminate against them. While it is rare to find such provisions in written contracts, the Commission's sweep may well have uncovered some. The Preliminary Report also notes a number of practices that may have a similar effect to territorial restrictions, such as the provision of less favourable warranties for products sold outside a retailer's home country. Such hardcore restrictions are the area most likely to see enforcement action from the Commission.

Digital content

In relation to digital content, the Preliminary Report limits itself to detailing the various commercial models covered by the questionnaire responses received from companies ranging from public service broadcasters to sports rights organisations and film studies. The Preliminary Report notes that digital content is the "key determinant of competition" in this area. As a result, it expresses concerns over the potential exclusionary effects of exclusive licensing and related contractual practices, which it concludes could cause and create significant barriers to entry for new market players.

The Commission also highlights the extent of territorial restrictions in this area, reflecting the fact that digital content distribution models are primarily based on national territories. The Preliminary Report finds that geo-blocking is a common practice in the online distribution of digital content, with 70% of all digital content providers using geo-blocking to restrict access to their digital content for users from other Member States. While the Commission clearly views such restrictions as a major barrier to the single market, the Preliminary Report draws back from taking a position on their compatibility with Article 101 TFEU. This is understandable, given the role played by (national) copyright laws, the wide variety of business models and content types covered, the complex ecosystem supporting the exploitation of content and the political sensitivity of this issue. Perhaps the most interesting point concerning online content, amongst the mass of data presented by the Commission, is the observation that purely online internet TV services comprise the most likely category of content retailer to acquire rights on a pan-European basis. Given that such services (which tend not to be European) are under regulatory attack in other areas, the recognition by the Commission that they are doing more than traditional media outlets to break down barriers to pan-European rights exploitation is notable.

Observations

The Commission has invited comments on the Preliminary Report, which must be submitted by 18 November. At a stakeholder day on 6 October, it opened the floor to various businesses and representatives with an interest in the sector inquiry's findings. Unsurprisingly, there was little consensus.

Although the Commission has described this sector inquiry as primarily a "fact finding exercise", it is important to note that past sector inquiries have been a prelude to enforcement action by the Commission, especially where this involved taking action on an

issue that had previously not been investigated (as was the case with 'pay for delay' cases after the pharmaceutical sector inquiry). While the legal framework governing online sales restrictions is largely settled, the Commission has been rather inactive in this area over recent years, with the exception of ongoing enforcement cases concerning the 'geo-blocking' of pay-TV services and online video game sales. This has meant that there have not been opportunities at an EU level to test the case by case approach to non-hardcore restrictions that was adopted in the Verticals Guidelines and, as a result, the safe harbour provided by the VBER has proved more absolute than the Commission suggested at the time.

At the moment, it is unclear whether the Commission will use the final report on this inquiry as the justification for a more interventionist approach and willingness to push the boundaries of the law (as, for example, the German Federal Cartel Office). This would require a greater willingness on its part to scrutinise non-hardcore restrictions such as platform sales bans, physical store requirements or other aspects of selective distribution that would otherwise be protected by the VBER. Alternatively, the Commission may limit itself to bringing cases against obvious infringements such as resale price maintenance or outright bans on online sales. Based on comments by the Commissioner on 6 October, the Commission sees the fact that many companies are already paying closer attention to ensuring that their existing agreements comply with the law as a desirable outcome in itself. Looked at in this light, the sector inquiry will already have achieved something even if no enforcement action follows. One way or another, however, once the final report is published next year enhanced enforcement, whether by the Commission or national competition authorities, seems inevitable. In the meantime, any companies doing business in the EU that are still imposing pricing or territorial restrictions, or prohibiting or discriminating against online sales, would be wise to review their current contracts before it is too late.