

# Capturing the Online Opportunities: Report on E-Commerce Provides Ammunition for the Review of Vertical Restraints

*Contributed by: Hanne Melin, Sidley Austin LLP*

The Internet continues to develop as a powerful distribution and communication channel. We have only seen a fraction of what it can be used for, but we know it is here to stay: "Internet use for retail shopping is destined to become pervasive."<sup>1</sup> This is beneficial to both European consumers and businesses. The European Commission's recently published report on cross-border e-commerce in the EU (E-Commerce Report)<sup>2</sup> finds that the Internet expands the size of the market and gives consumers access to more providers and more choice.

But the E-Commerce Report also identifies existing barriers that are holding back efficient and EU-wide online retailing. Selective distribution law is mentioned as one of these barriers. This area of law falls within the Vertical Restraints Regulation (VRR)<sup>3</sup> which expires in May 2010 and is therefore currently being reviewed by the Commission.

It is clear that the VRR can play an important role in creating the right incentives for companies to explore online channels. This short article suggests that the Commission must now build on the findings of the E-Commerce Report and ensure that the new VRR regime promotes market integration and furthers consumer choice.

## *Existing Barriers*

On the basis of fact-finding interviews with business stakeholders and trade associations, the E-Commerce Report identifies several barriers hindering the development of EU-wide online retailing. There are already proposals to tackle some of these barriers, such as the Consumer Rights Directive and a future Communication on retail monitoring. The review of the VRR is also a timely opportunity to ensure that competition rules contribute to bringing down e-commerce barriers.

In short, the VRR exempts certain types of vertical agreements from the prohibition against agreements that restrict competition (this prohibition is found in Article 81(1) EC Treaty). Only agreements which can be presumed to create countervailing efficiencies from which consumers receive a fair share are exempted under the VRR.

Selective distribution is one of the agreement types exempted under the VRR. Selective distribution means that the supplier appoints retailers on the basis of certain criteria. These criteria must be qualitative, objective, non-discriminatory and proportionate and will normally relate to product presentation, staff qualifications, *etc.* The appointed retailers are prohibited from selling to unauthorised retailers, but they must be allowed to sell to other appointed retailers and to consumers wherever situated in the EU. The appointed retailers must also be allowed to sell using the Internet.<sup>4</sup> The supplier can control the quality of the online operations by imposing criteria, just as he can do in relation to the retailers' traditional retail operations.

Problems arise when such criteria go beyond what is necessary *e.g.*, proper product presentation online or when they discriminate against certain or all online channels (the E-Commerce Report talks about "supply-side . . . constraints" holding back efficient European online retailing).<sup>5</sup> Examples would include criteria that: prohibit approved retailers from setting up their webshop on a third-party online platform; require them to also operate a brick-and-mortar shop; require them to make no more than a set percentage of turnover from online activity or limit the number of units they sell to a single online customer; prohibit them from selling certain models or product lines on the Internet; or require them to comply with certain conditions which make online selling too expensive or too difficult to actually engage in.

## *Opportunities Ahead*

The opportunities identified by the E-Commerce Report as flowing from efficient and EU-wide online retailing fit entirely with the objectives of EU competition policy – namely market integration and consumer welfare in terms of real consumer choice.

### Expanded and Integrated Markets

The Internet is an efficient tool to overcome obstacles to market integration. It has the potential to enable consumers to shop around for better deals, it can increase the competitive pressure on prices across borders and in traditional retailing, and it can increase quality and choice as consumers are able to obtain products not available in their own country.<sup>6</sup> For consumers in smaller and/or insular Member States, the Internet can play a key role in that consumers rely on it for accessing products not available nationally. For example in Malta, Luxemburg and Cyprus, cross-border e-commerce has already outpaced domestic e-commerce.<sup>7</sup>

The Internet also provides suppliers and retailers with an opportunity to penetrate established markets and open up new ones. Here, third party online platforms provide great assistance. First, online platforms enable retailers to set up safe online operations at a lower cost and to more easily profit from online benefits such as economies of scale, efficient distribution, reduced necessary stock levels, *etc.* Second, online platforms make retailers more visible and accessible to consumers. This all leads to price savings for consumers. An independent study by Frontier Economics (commissioned by eBay) estimates that consumers on eBay's European platforms benefit from individual savings of 17 percent per transaction, and total savings of around €1.1 billion per year.

The Internet can thus act as an effective force for social cohesion and market integration. The VRR must ensure retailers and consumers are able to take full advantage, irrespective of the type of online channel used. Third-party online platforms are, for instance, popular among consumers, lead to price savings and are perfectly capable of being used to sell products in enhanced conditions. Suppliers who outright prohibit appointed retailers from using online platforms, *a priori* ban an entire distribution channel. In fact, they prevent retailers from demonstrating that their online shops, set up on a third-party online platform, are capable of satisfying the supplier's quality criteria. It is important to understand that it is not the distribution channel but the retailer who should satisfy the supplier's criteria – it is in this respect irrelevant whether the distribution channel is a department store, a supermarket or an online platform.<sup>8</sup>

### Greater Consumer Choice

“The Internet gives more power to the individual than any technological change in history” – these words of Commissioner Kroes<sup>9</sup> are backed up by the E-Commerce Report. The report finds that the Internet has dramatically widened consumer choice: consumer choice and price visibility on the Internet are vast compared to a local store.<sup>10</sup> And as noted by *Which?* (the UK consumer organisation) in its submission to the Online Commerce Roundtable,<sup>11</sup> consumers are willing to purchase almost anything online when given the choice.

Clearly, we see that online retailing has the potential to increase consumer welfare. It enables consumers to obtain products not available in their own country, and increases the competitive pressure on inefficient retailers. Consumers are increasingly using the Internet to inform themselves before purchasing a product not only online but also from traditional channels. Consumers find both price and quality comparisons to be easier online. Moreover, consumers are on average more satisfied with online channels than with other retail channels.<sup>12</sup> On the Internet, they find a wider range of offers in terms of innovation, price and quality; they can more easily see and compare prices; and they can shop without being limited by opening hours.<sup>13</sup>

The Internet thus creates high expectations on the part of consumers in terms of access and choice when shopping. The VRR must ensure that retailers are able to meet such expectations, and this is impossible if retailers are forced to limit their online operations. For example, requirements that prohibit certain (often attractive and new) product models or collections from being sold on the Internet or that put a cap on the revenue the retailer can generate online, effectively hold back the full potential of the Internet. The same is true of requirements that online retailers must also operate offline. Retailers who are perfectly capable of satisfying quality standards, but do not have the means, possibility or desire to operate on the high street, are foreclosed. Consequently, consumers are limited in their choice of products and services.

### *Conclusion*

Consumer behaviour is changing. Consumers increasingly turn to online channels (from 22 percent in 2004 to 32 percent in 2008), and they are satisfied when doing so (overall satisfaction is 85.9 percent online compared to 75.8 percent on average for all sales channels).<sup>14</sup> However, there are barriers preventing consumers from taking full advantage of the Internet. The abuse of selective distribution is identified as one such barrier, and this is a signal to the Commission: the Commission should use the review of the VRR to ensure that the EU puts in place an instrument that promotes efficient and EU-wide online retailing to the benefit of consumers.

The new VRR regime must support retailers who want to grow successful online businesses. It should recognise the individual as well as the complementary nature of different online channels, the ability of online retailers to offer services that are valuable to consumers, and the potential of the Internet to strengthen both offline and online competition.

*Hanne Melin is an associate in the EU competition law practice of Sidley Austin LLP based in Brussels. She has assisted eBay on EU law matters, but the views expressed in this article are her own, not those of Sidley Austin LLP or eBay. This article has been prepared for academic purposes only and does not constitute legal advice. Telephone: +32 2 504 6451, Email: hmelin@sidley.com.*

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<sup>1</sup> Comment by Consumer Commissioner Meglena Kuneva. See Consumers: Online shopping increasingly popular in the EU, but development “held back” by barriers to cross border trade – European Commission Press Release, IP/09/354 of 5 March 2009.

<sup>2</sup> Commission Staff Working Document – Report on cross-border e-commerce in the EU, SEC(2009) 283 final, 5 March 2009.

<sup>3</sup> Regulation 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices, OJ L 336/21, 29.12.1999. The VRR expires on 31 May 2010, and the Commission is currently reviewing it with a view to replacing it.

<sup>4</sup> See paras 51 and 53 of Commission Notice – Guidelines on Vertical Restraints, OJ C 291/1, 13.10.2000 (Vertical Guidelines).

<sup>5</sup> See pp. 3, 16, 18-20 of E-Commerce Report.

<sup>6</sup> *Id.* at section 4.

<sup>7</sup> *Id.* at p. 8 and Figure 5 (Annex 1).

<sup>8</sup> For example, in Case 107/82 *AEG v Commission* [1983] ECR 3151, the Court explained that “a manufacturer who has introduced a selective distribution system cannot therefore absolve himself, on the basis of an a priori evaluation of the characteristics of the various forms of distribution, from the duty of checking in each case whether a candidate for admission satisfies the specialist trade conditions” (para. 75).

<sup>9</sup> Closing remarks by Commissioner Kroes at Online Commerce Roundtable, 17 September 2008.

<sup>10</sup> See p. 17 of E-Commerce Report.

<sup>11</sup> Available at: [http://ec.europa.eu/competition/sectors/media/which\\_contribution.pdf](http://ec.europa.eu/competition/sectors/media/which_contribution.pdf).

<sup>12</sup> See section 5.1 of E-Commerce Report. A survey commissioned by the Commission looked at two consumer product categories considered representative for assessing consumer satisfaction with the internet as a retail channel – namely “Entertainment & Leisure” products and “Information & Communication Technology” products.

<sup>13</sup> Looking at the survey’s results regarding Entertainment & Leisure products, consumer satisfaction was higher online as regards overall satisfaction (85.9 percent of consumers online compared to 75.8 percent of consumers on average for all sales channels), quality and price (80 percent vs 67.3 percent), and quality of services (75.3 percent vs 72.7 percent). Satisfaction is also higher for online purchases with regard to innovation, ease of purchase, opening hours, price transparency, affordability, choice of qualities, price comparability, range of prices, and fulfilment of delivery. (See figures 6-15 (Annex 1) of E-Commerce Report.)

<sup>14</sup> *Id.* p. 5 and 10.