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Avoiding Antitrust and Competition Pitfalls When Distributing in the U.S. and Europe

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- Robert Bell has over 30 years of experience advising on complex competition and regulatory matters in London and Brussels involving some of the leading cases before the Competition and Markets Authority, the European Commission, and U.K. and European Courts. He is qualified to practice in both England and Wales and Ireland. He advises clients on a range of competition law issues including merger control, cartels, restrictive practices, distribution issues, competition litigation, national security clearances and public procurement law. He has also regularly advised clients on sectoral regulation (e.g. digital platforms, telecoms, medical devices, energy) and trade law including economic sanctions, export controls and customs issues.
- He is a former Chair and now Member of the City of London Law Society's Competition Law Committee, which liaises with the U.K. Government and the EU and U.K. competition regulators in connection with the reform of competition law and practice. Robert is recognised as one of London's leading lawyers by Chambers U.K. and The Legal 500 U.K.

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- Steve Foristal, a member of the firm's Corporate Services practice group, primarily focuses on mergers and acquisitions and commercial transactions. For public and private companies of all sizes, Steve provides counsel on pre-transaction planning and negotiations of letters of intent; due diligence investigations and data room management; drafting and negotiation of key transaction and closing documents; and coordination and management of transactions from inception through post-closing.
- Steve regularly counsels both public and private companies on antitrust compliance issues under the Sherman Act, Clayton Act, Federal Trade Commission Act and applicable state laws, such as distribution, dealer, exclusivity and supplier issues, price discrimination, discounts, rebates, minimum advertised price policies and most favored nations pricing issues, Hart-Scott-Rodino Act filings, internal audits, trade associations, tying, monopolization and other antitrust compliance issues.

Agenda

- Introduction
- Comparative approach of U.S. antitrust /competition law to distribution issues
- Structuring your distribution chain
- Resale pricing; Minimum Advertised Price Policies
- EU developments in e-commerce /online selling
- Discounts and marketing allowances
- Territorial and customer exclusivity
- Noncompete restrictions
- Best Price / Most-Favored Nation Clauses
- Key takeaways

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U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

- Purpose: promote consumer welfare through effective competition.
- Competition is protected by prohibiting:
 - conspiracies in restraint of trade
 - unreasonable restrictions on purchasers and suppliers
 - excessive concentrations of economic power
 - other anticompetitive practices
- Legal penalties to punish violators and deter future violations

U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

▪ Driven by Economics –

- Free enterprise economy uses competitive markets to allocate goods and services
- When the forces of supply and demand work freely in open markets, consumers receive:
 - The best quality products/services
 - At the lowest possible prices
- Competition spurs economic performance
 - Promotes efficiency, creativity and innovation
- Monopolies, market concentration and collusive conduct inhibit competition and reduce market performance

U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

▪ Enforcement Mechanisms

- Department of Justice - Antitrust Division
 - Criminal enforcement
 - Civil enforcement
 - Pre-merger review
- Federal Trade Commission
 - Civil enforcement - FTC Act
 - Pre-merger review
 - Consumer protection
- State Attorneys General
- International Regimes
- Private Enforcement
 - Treble damage civil litigation
 - Class actions



U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

■ Penalties can be severe

- Companies convicted of antitrust violations pay very large fines
 - Up to \$100 million (can be more depending on damages proven)
- Individuals convicted serve actual jail time and pay substantial fines
 - Up to \$1 million (more if damages proven) and 10 years in prison
- Debarment from federal and state programs
- Defending antitrust claims is very costly / drains resources
- Civil actions may result in 3x actual damages plus payment of adversaries' attorneys fees



U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

▪ Key Statutes

- Section 1 of the Sherman Act
 - Prohibits agreements that restrain competition
 - Elements:
 - Two or more entities
 - An express or implied agreement
 - An unreasonable restraint on competition
 - » Proved – Rule of Reason (actual and substantial lessening of competition)
 - » Presumed – Per Se (Automatic) liability
- Section 5 of the FTC Act
 - Government (FTC) enforcement only
 - FTC expanding application and theories of liability
 - Broadly proscribes acts of “unfair competition”
 - Concurrent with other antitrust laws (e.g. Sherman Act)

U.S./EU Antitrust/Competition Approach to Distribution Issues – U.S. Approach

▪ Key Analytical Structures

- **Per Se Illegality** – Illegal agreements among competitors
 - Price fixing; customer/geographic market division; group boycotts; bid rigging
- **Rule of Reason** –
 - Generally applies to vertical agreements
 - Balance procompetitive benefits of an agreement against anticompetitive harm
 - Many purely vertical agreements are upheld under these tests, including many common terms in distribution agreements
 - Makes the risk profile in the U.S. generally lower than many other jurisdictions for many types of vertical restraints
 - BUT, balancing structure can make it somewhat unpredictable
 - Prevalent private enforcement (including class actions) makes it easier to challenge these agreements in the U.S. than in some other jurisdictions

U.S./EU Antitrust/Competition Approach to Distribution Issues – EU Approach

- Two broad-based prohibitions; anticompetitive agreements between undertakings (Article 101 TFEU) and abusive conduct by undertakings in a dominant position (Article 102 TFEU)
- Enforced by EU Commission or national competition authorities
- Sanctions for breach; substantial fines (10% of worldwide turnover), unenforceability of agreements, cease and desist orders, damages actions
- No rule of reason but can assess whether anticompetitive agreement merits an individual exemption (Article 101(3) TFEU)
- Safe harbour legislation for Vertical Agreements (Commission Regulation 2022/720) (“**Block Exemption**”) and Vertical Agreements Guidelines (“**Guidelines**”)

U.S./EU Antitrust/Competition Approach to Distribution Issues – EU Approach

- **Strict enforcement against restrictions in vertical agreements between suppliers and distributors**
- **Emphasis on promoting intra-brand competition as well as inter-brand competition due to need to create EU Single Market**
- **More balanced approach towards imposing restrictions on online selling under Block Exemption and Guidelines**
- **Companies and their lawyers try to ensure their vertical agreements fall with the Block Exemption for sake of legal certainty**
- **Block Exemption applies if both parties have under 30% market share and do not contain hardcore restrictions (e.g. RPM, restrictions on customers/territories to be served, preventing effective use of internet)**

Structuring Your Distribution Chain: U.S. Perspective

- **Direct to Consumer**
 - Employees, salaries, training, overhead, compliance, etc.
 - Most control
- **Sales Representatives**
 - Independent contractors (not agents)
 - Market, promote, and solicit the sale of products to potential end users in specified territories
 - Commission, not salary
 - Supplier controls end user sale terms (accept order; pricing; T/Cs; etc.)
 - Supplier retains credit and inventory risk (diff. from agency)
 - Somewhat less control

Structuring Your Distribution Chain: U.S. Perspective

▪ Distributors

- Typically buys (takes title) to products (inventory) from supplier (e.g. manufacturer; wholesaler) and resells them to other parties in the supply chain, such as resellers and end users
- Separate contracts with supplier and its customer (hence, vertical restrictions)
- Often provide (procompetitive) services for the supplier, such as product marketing, inventory management, warehousing and post-sale support services
- Bear credit risk and inventory risk
- Inherent antitrust risks (e.g. vertical restrictions)
 - Also: Termination protections? Franchise? Dealer laws (e.g. auto; gas)?
- Lower control, but cover via (permissible) contractual requirements / restrictions

Structuring Your Distribution Chain: EU Perspective

- **What do you want from your indirect channel (geographic coverage v control)?**
- **Wholesaler:** suits new entrant into EU market relying on wholesaler with own Different types of distribution network. Can stop wholesaler selling to end users. Bears risk of the transaction.
- **Exclusive Distributor:** suit more sophisticated exporter willing to invest time in developing network: appoint to distribute within a given territory or customer group; can reserve key accounts to supplier; stop active sales outside territory into other exclusive territories. Bears risk.
- **Selective Distribution:** suit distributor of luxury or complex products, appointment of distributors meeting key qualitative criteria, distributors can only sell to end users or other authorized dealers; greater control cuts out discounters. Bears risk.
- **Non-Exclusive Distributor:** least restrictive, can have multiple distributors, can stop active sales into exclusive distributor or selective distributor territories. Bears risk.
- **Agency:** appointing a genuine agent to sell on suppliers' behalf for a commission, largely fall outside competition rules and can dictate resale prices and conditions of sale. Limitations on agents who sell for multiple brands and those on digital platforms treated as distributors. Watch out for compensation rights upon termination of selling goods. Agent bears no economic risk.

RPM and MAP Pricing: U.S. Rules

▪ RPM = RESALE PRICE MAINTENANCE

- Supplier Sets Distributor's / Reseller's (Minimum) Resale Price (i.e. Vertical Price Fixing)
- Rule of Reason under Federal Law (per US Supreme Court's 2007 decision in *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*)
- Procompetitive benefits courts consider include:
 - Encouraging resellers to make investments in tangible and intangible services, such as:
 - high-quality displays or showrooms;
 - product demonstrations and other initiatives to educate customers; and
 - good customer service.
 - Making it easier for new brands to enter the market because a minimum RPM agreement can encourage retailers to promote the new brand to customers who are unfamiliar with it by increasing their margins.
 - Preventing free-riding on the investments made by high-service retailers by discount or internet retailers (e.g. a shopper goes to a store to learn about different products from a sales associate and then leaves to buy the product for less online).
 - Allowing manufacturers to maintain a premium-brand image if they choose, increasing the range of options for consumers.

RPM and MAP Pricing: U.S. Rules (RPM Cont.)

- **Potential anticompetitive harms courts consider include:**
 - Facilitating a manufacturer or retailer cartel.
 - Allowing a powerful manufacturer to refuse to reduce prices to retailers that might otherwise be passed on to consumers.
 - Allowing a powerful retailer to protect itself from competition with more efficient rivals.
- **BUT, state laws can be more restrictive than federal; Minimum RPM agreements may remain per se illegal or unenforceable in states where:**
 - State courts do not always follow federal decisions in interpreting their own antitrust laws (e.g. CA courts and AG are hostile to Minimum RPM).
 - State legislatures have passed statutes expressly rejecting Leegin (e.g. MD).
 - State laws otherwise ban RPM agreements or render them unenforceable (e.g. NY).

RPM and MAP Pricing: U.S. Rules

Minimum Advertised Price Policies

■ MAP = MINIMUM ADVERTISED PRICE POLICIES

- Increasingly Common Alternative to Minimum RPM Agreements
- Restrict minimum ADVERTISED price, but not RESALE price
- Typically unilateral POLICIES, not AGREEMENTS
- Escalating consequences for violations (e.g. “do not ship” list; termination)
- Very common for online retailers (actual resale price displayed after placed in shopping cart)
 - Issue: When does the “advertised” price become the “resale” price?
Not yet tested in court
- Difficult to challenge under Rule of Reason; challenges tend to rely on disguised horizontal conspiracies

RPM and MAP Pricing : EU Rules

- RPM restriction on distributor's freedom to determine resale price of goods purchased from supplier is a serious restriction of competition law
- RPM includes direct or indirect means of setting fixed or minimum prices such as setting margins, price tracking, price monitoring mechanisms
- **ALLOWED TO** specify maximum resale prices or recommend resale price as long as not enforced by incentives or retaliation
- MAP policies (restriction on advertising prices below a minimum level) are treated by EU Commission as an indirect means of applying RPM and a serious restriction of competition

EU Developments in E-Commerce/ Online Selling

- Block Exemption and Guidelines take a new more balanced attitude to online sale restrictions
- Any restrictions which prevent the effective use of the internet by buyer are serious restrictions of competition (no blanket or conditional bans on use of internet)
- Can impose quality requirements for online sales applies in objective transparent and non discriminatory way (e.g. particular appearance of goods on buyers online store or requirements relating to display of the goods, way suppliers trademark is used, operate at least one brick-and-mortar store)
- Can ban buyers using online marketplaces
- Can provide that distributor sells a specific amount (not percentage) of goods offline
- Can stop buyers using services of particular advertising providers that don't meet quality standards
- Impose an obligation not to use suppliers brand name in the domain of own online store
- However you cannot ban the use of an entire advertising channel (e.g. price comparison sites) as it increases consumer search costs and softens retail price competition
- Possibility of introducing dual pricing of wholesale prices charges to distributors to take account of extra costs/investments of a specific channel of distribution (e.g. investment in brick-and-mortar stores)

U.S. Discounts and Marketing Allowances – Price Discrimination

- **Robinson-Patman Act is the primary price discrimination statute in the U.S. (U.S. government no longer actively enforces, but private parties can and do)**
- **Purpose: Help smaller retailers compete against larger ones (e.g. “big box”) who can obtain better pricing from sellers. Prohibits sellers from treating competing customers differently as to:**
 - Prices
 - Terms of sale
 - Marketing support
- **To prove a price discrimination claim, a plaintiff must prove:**
 - A difference in price
 - Two or more contemporaneous sales in interstate commerce
 - Sales by the same seller to two or more different competing purchasers
 - Sales of goods of like grade and quality
 - A competitive injury
- **Three statutory defenses against claims of price discrimination:**
 - Cost justification (Volume discounts?)
 - Meeting competition
 - Changed conditions
- **Courts have created an additional defense – the “functional availability” defense**

U.S. Discounts and Marketing Allowances – Loyalty and Rebate Programs

- Price discounts or favorable financial terms in return for a customer's purchasing commitment
- Generally viewed favorably as a form of price competition
- Antitrust claims typically rely on related theories, such as:
 - Improper exclusive dealing (discussed later)
 - Illegal tying or bundling (discount for one product if the customer also buys a second product)
 - Predatory pricing (pricing below cost to eliminate a competitor from the market)
 - Price discrimination
 - Attempted monopoly

EU Discounts and Marketing Allowances

- Non-dominant companies are free to a large extent to offer what discounts and allowances they wish to their customers.
- Dominant companies have extra responsibilities to ensure they do not discriminate between purchasers in similar situations; if offering different discounts offered for similar transactions must be objectively justified, linked to cost savings and applied in a uniform manner.
- Exclusivity or loyalty rebates need careful analysis for dominant companies.
- Companies can provide marketing support allowances to distributors which take on marketing activities which would otherwise be down to the supplier.
- Marketing allowances to support dealers who maintain a brick-and-mortar presence are permitted if they are for an absolute figure and are not pegged to the number of offline sales made.
- **Note:** New rules now allow dual pricing between online/offline sales in appropriate circumstances.

Territorial and Customer Exclusivity: U.S. View

- **Manufacturer limits retailer's or distributor's sales to a particular geographic territory or to a particular category of customers**
 - Reserve to itself certain geographies or customers, such as government or national accounts
 - Prevent distributors from selling to other wholesalers or retailers
- **Can also involve exclusive dealing / purchase and sale (unilateral or mutual)**
- **Rule of Reason**
 - Whether there are legitimate business justifications for the restraint
 - The overall impact on competition in the relevant market
 - The impact on inter-brand competition (among competitive brands)
 - The impact on intra-brand competition (among retailers within a single brand)
 - The market share or market power of the supplier in the relevant market

Territorial and Customer Exclusivity: U.S. View

- **Because inter-brand competition is the primary concern of US antitrust law, restraints typically upheld**
- **Significant potential procompetitive benefits:**
 - Providing assurance of supply for retailers and outlets for distribution for suppliers
 - Enhancing the ability of both parties to plan
 - Improving quality and supervision of distributor or retailer services
- **Potential anticompetitive effects:**
 - Foreclose competitor(s) from accessing the market (e.g. eliminating access to powerful distributor or retailer)
 - Not dispositive, but foreclosure of less than 30% of the market is generally not problematic
 - If harm to intra-brand competition outweighs benefits to interbrand competition (e.g. competitors' products are very different from the supplier's)
 - The restraints are not needed to accomplish the proffered business justifications

Territorial and Customer Exclusivity: EU View

- Block Exemption allows suppliers to impose territorial and customer exclusivity on buyers in certain circumstances
- You can appoint up to five distributors as exclusive within a given territory
- You can stop distributors actively selling into an exclusive geographic territory or an exclusive customer group allocated to a particular distributor or to the supplier
- Applies also to protect selective distribution system in other territories
- A supplier can reserve certain key accounts to itself even if it appoints a distributor as exclusive
- You cannot ban passive sales (where customers order from buyers without solicitation)
- Selling on the internet is considered passive selling

Noncompete Restrictions: U.S. Perspective

- Prohibits the distributor from selling competitive products during the agreement term (sometimes for a specified period after termination)
 - Similar to exclusivity restrictions
- More commonly challenged under specific state “restrictive covenant” statutes – highly fact-specific cases. Courts consider:
 - The industry at issue and the reasonableness of the provision in terms of its duration, geographic scope and scope of restricted activities
 - Whether the provision is ancillary to a valid transaction and supported by adequate consideration
- Most noncompete agreements are void under California law (use confidentiality and trade secret protections to get similar outcome)

Noncompete Restrictions: EU Perspective

- For the purposes of the Block Exemption, a restriction on a buyer not to manufacture or sell competing products or to obtain from the supplier 80% or more of the distributor's requirements is treated as a noncompete clause under EU law.
- To come within Block Exemption, noncompete clauses must not last longer than five years. Can be renegotiated but cannot automatically roll over. Evergreen clauses regarded as indefinite. However, new Guidelines suggest it can go beyond five years as long as no restriction on buyer terminating.
- Any infringing clause will fall outside the Block Exemption and will need to be individually assessed under individual exemption procedure.
- Cannot have a post-termination noncompetition clause except in franchising agreement and in agency agreement.

U.S. Best Price / Most-Favored Nation Clauses

- **Supplier agrees to treat a particular customer no worse than all other customers (e.g. price no higher than to other buyers)**
 - Reduce uncertainty about potential price fluctuations
 - Reduce the transaction costs of both initial and later bargaining
- **Usually ok, but antitrust concerns when used:**
 - By companies with dominant market shares to monopolize or maintain market power
 - As part of a broader collusive scheme
 - E.g. health insurance industries agreeing to MFN's with substantial percentages of providers, thus reducing incentive of providers to negotiate or compete on price (knowing the other providers will get the benefit of the same price from the insurer)

EU Best Price / Most-Favoured Nation Clauses

- Different types of Best Price /MFN Clauses
- Parity /MFN clauses require a seller of goods or services to offer the goods or services to another party on condition that they are no less favourable than the conditions offered by the seller to certain other parties via its own direct sales channels (e.g. own website) (“narrow”) or via all other channels (“wide”).
- The conditions may concern prices, inventory, availability or any other terms or conditions of offer or sale.
- The parity obligation may take the form of a contractual clause, or it may be the result of other direct or indirect measures, such as differential pricing or other incentives. These can still fall within the Block Exemption.

EU Best Price / Most-Favoured Nation Clauses

- **Retail parity obligations** relate to the conditions under which goods or services are offered to end users. These obligations are often imposed by providers of online intermediation services (for example, online marketplaces or price comparison services) on the buyers of their intermediation services (for example, undertakings that sell via the intermediary platform)
- Narrow retail parity obligations refer to the conditions offered on the direct sales channels of sellers of goods or services. Wide retail parity obligations refer to the conditions offered on all other sales channels.
- **Particularly offensive are retail parity obligations** which cause a buyer of online intermediation services not to offer, sell or resell goods or services to end users under more favourable conditions via competing online intermediation services, (so called **across platform retail price parity clauses**) are **excluded from the protection of the Block Exemption**.

Key Takeaways

- Violations can result in substantial financial and criminal penalties
- Agreements among competitors can be per se illegal
- Vertical relationships with customers and suppliers – more flexible in U.S., stricter in EU
- EU now has a more lenient regime for imposing restrictions on online selling, but not a green light to ban internet selling for fixing resale prices
- Antitrust/competition laws can be technical and confusing – seek antitrust/competition counsel for assistance as appropriate

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- Code Word: **PITFALL**



QUESTIONS



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