COUNTDOWN | 22 March 2022

Distribution Law Center Countdown XIV - Active sales restrictions (Rolling over prohibition)

What?

Classic notions in the world of vertical agreements are those of “active sales” and “passive sales”. Active sales involve some form of active targeting of a particular customer group or territory. Passive sales consist of transactions in response to unsolicited requests from individual customers without having initiated the sales by means of active targeting of such customers.

In order to protect efforts and investments made by exclusive, but non-selective distributors, the block exemption regime accepts under strict conditions that other distributors may be obliged to refrain from active selling into the territory or to a customer group that is allocated to an exclusive distributor. Passive sales by such other distributors are however always blacklisted.

This countdown deals with the last of three conditions (the rolling over prohibition) that must be met to render active sales restrictions compatible with the block exemption and thus to be automatically exempted under the EU competition rules. Given the complexity of the matter, the two other conditions (the exclusivity requirement and the parallel imposition requirement) have been addressed in the two previous countdowns no. 12 and 13.

Now?

The current Vertical Block Exemption Regulation (the “VBER”) places the imposition of restrictions on active and passive selling in principle on the black list. There is however a limited exception, that is subject to stringent cumulative conditions.

The first condition is that the active sales restriction must target a territory or a customer group that is either reserved to the supplier or exclusively allocated to a particular (single) distributor (see DLC countdown no. 12). This is referred to as the “exclusivity condition”. The second condition requires that the active sales restriction is imposed on all of the buyers of the supplier (including all of the companies belonging to the same group of companies) (see DLC countdown no. 13). This is called the “parallel imposition requirement”.

The third condition is that the active sales restriction can only be imposed on the (direct) buyer of the supplier. This will typically be the distributor appointed by the supplier. The supplier is not entitled to require from its distributor that it imposes, in turn, an active sales restriction on its own customers. Hence the imposition of an

obligation on distributors to roll over the active sales restriction to the next level is not compatible with the block exemption of active sales restrictions. This is typically referred to as the “rolling over prohibition”.

The future as of 1 June 2022?

The Commission proposals amend the third condition.

The proposals entitle the supplier to require that an active sales restriction is imposed also on the customers of a party that was given distribution rights by the supplier. This means that a supplier can require from its distributors that they pass on or roll over the active sales restriction to the next level.

The text seems to suggest that this passing on or roll-over possibility is limited to one level. In other words, the supplier cannot require that its distributor imposes an active sales restriction on its immediate customer *and*, in addition, require that these customers must also impose the active sales restriction on their customers.

This may all sound complicated and that is also what it is. A practical example may clarify matters.

In practice?

Imagine that a producer of high-tech TV-sets appoints an exclusive distributor in each major city of the EEA countries. The producer requires particular investments and efforts of these distributors for which the producer wishes to offer some form of contractual protection. The protection takes the form of active sales restrictions that are imposed on the various distributors. Exclusive distributors are protected against active marketing by other distributors within their city. Under the current regime, it is possible that the distributor sells the TV-set to a trader in his city and such trader can then not be held to any active sales restriction. In other words, the supplier cannot require that his distributors impose the same active sales restriction on their customers (here: the trader).

This is changed in the current proposals. The supplier can require that the distributors pass on or roll over the active sales restriction to their customers. If that happens, the distributor in our example must impose the same active sales restriction on the trader. This implies that the trader will be contractually prevented from making active sales in other cities in which an exclusive distributor has been appointed.

Assessment?

The creation of room to pass on or roll over active sales restrictions provides a response to the concerns expressed in the Expert Report. The Expert Report emphasized that in many real life scenarios the current regime is impractical and ineffective. Several Distribution Law Center contributors provided concrete examples of

scenarios where, without such a passing on or roll over possibility, protection against freeriding is simply not working. The concerns applied in particular in the context of distribution set-ups that are not homogenous, e.g. with wholly owned importers in some Member States and independent importers in other. The proposals address also the concern that it is easy to circumvent the active sales restriction by making use of a reseller or trader who then in turn is free to engage in active selling wherever he wants.

The formulation in the current proposals may trigger interpretation difficulties. The passing on is only allowed with regard to customers of "a party that was given distribution rights by the supplier". There is no doubt that this applies to distributors appointed by the supplier directly. However, how about the customers of a distributor appointed by an independent importer which in turn is appointed by the supplier? Are the customers of the distributor customers of "a party that was given distribution rights by the supplier"? The same question applies one level down. Imagine that the distributors of the supplier work with sub-distributors. Is it possible to extend the obligation to impose the active sales restriction to customers of the sub-dealers? Hopefully the definitive version of the new Vertical Guidelines will clarify the position in this respect. We find ourselves in a hardcore environment where legal certainty is essential.

Want to know more? Stay tuned...

Counting down towards 1 June 2022 we aim to provide you with regular updates and the necessary legal knowhow in order to fully prepare your business for the future. Please also check out the Distribution Law Center platform and our LinkedIn page for much more information on the laws governing vertical agreements, covering both competition and commercial law. 27 specialized teams from all over the EEA are working hard to turn the platform into your favourite source of guidance and information.

A translation of this Countdown newsletter is available in the following languages: Croatia, Czech, Portuguese, Romanian, Slovakia, Swedish.

Read the available DLC Countdown newsletters on the changes to be expected here.