Distribution Law Center
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Distribution Law Center Countdown XIX - Selective distribution

What?

One of the common types of distribution agreements are selective distribution agreements. In a system of selective distribution, the supplier undertakes to sell the contract goods or services, either directly or indirectly, only to distributors selected on the basis of specified criteria and these distributors undertake not to sell such goods or services to unauthorised distributors within the territory reserved by the supplier to operate that system.

By way of selective distribution, a supplier thus creates a network of authorised distributors. The admission to the network can be subject to purely qualitative criteria only, or additionally to quantitative criteria, which limit the potential number of distributors more directly by, for instance, requiring minimum or maximum sales or fixing the number of distributors.

Now?

Both purely qualitative selective distribution and quantitative selective distribution are covered by the Vertical Block Exemption Regulation ("VBER"), regardless of the nature of the products and the nature of the selection criteria.

For purely qualitative selective distribution, relying on the VBER may not even be required: if the selective distribution system complies with the so-called *Metro* criteria laid down by the European Court of Justice, it is generally considered to fall outside Article 101(1) TFEU. For this to be the case, the distributors must be selected only on the basis of objective criteria, required by the nature of the product, which do not put a direct limit on the number of distributors. Only then will the selective distribution system be considered to be purely qualitative of nature.

Under the VBER, the supplier must, in the territory where it operates selective distribution, prohibit its authorised distributors from selling to unauthorised dealers. This belongs to the essence of selective distribution and is not considered to be a hardcore restriction. Besides this, however, the authorised distributors operating at the retail level must be entitled to sell, actively and passively, to all end users in the "selective territory" and also to other members of the network. The latter cross-supplies between the members of the network must be allowed at all times, even between members operating at different levels of trade. Like in other distribution systems, the supplier

is entitled to prohibit authorised wholesalers from selling, actively or passively, to end users, and the supplier can impose a location clause on the members of its network, thus making sure that they operate from a given place of establishment. Finally, the Commission imposes an overall equivalence requirement on the criteria that apply to online and offline sales: compared to the latter criteria, the former may not dissuade distributors from using the internet.

The supplier is allowed to impose an active sales restriction on the members of its network outside the selective territory, to territories in which the supplier has appointed an exclusive distributor (Vertical Guidelines, no. 56). Inversely, selective distributors are not protected against active or passive sales by (exclusive) distributors located outside the selective territory into the selective territory.

The future as of 1 June 2022?

The draft VBER and draft Vertical Guidelines contain some important developments in respect of selective distribution.

The draft VBER expressly distinguishes between hardcore restrictions in three types of distribution systems: exclusive distribution (Article 4(b)), selective distribution (Article (4(c)) and distribution which is neither exclusive or selective (Article 4(d)).

In order to analyse the impact of the list of hardcore restrictions on selective distribution, account must be also be taken of the list of hardcore restrictions for the non-selective distribution. This shows that the draft VBER grants the authorised distributors, which often invest in the supplier's brand, enhanced protection against sales by unauthorised distributors.

The draft VBER does so in two ways. Firstly, the supplier will be allowed to prohibit sales to unauthorised distributors in the selective territory not only by the authorised distributors themselves, but also by their customers (Article 4(c)(i), second indent). Secondly, the supplier will be allowed to impose a restriction on (exclusive) distributors and/or their customers outside the selective territory to sell actively or passively to unauthorized distributors located inside the selective territory (Article 4(b)(ii) and 4(d)(ii)). This "reverse protection" is separately dealt with in the next DLC countdown 20.

The draft Vertical Guidelines, in their turn, provide more flexibility in defining the online criteria. The Commission indeed no longer imposes an overall equivalence requirement on the criteria that apply to online and offline sales. A supplier will be allowed to have different online criteria, provided that these do not have as their object to prevent the authorised distributors or their customers from effectively having online sales.

In practice?

Practitioners have long struggled with the creation of or the transition to a system of selective distribution in the EU, particularly because they have to apply an all or nothing approach. If selective distribution is not immediately applied throughout the EU, which frequently is the case for SMEs, the supplier is currently not allowed to protect its authorised distributors against sales by distributors located outside the selective territory to unauthorised distributors in the selective territory. Imposing a prohibition on such sales currently amount to imposing an illegal customer/territorial restriction on the latter distributors. The draft VBER remedies this and allows the gradual rollout of selective distribution in the EU.

Assessment?

The upcoming changes of the draft VBER and the Vertical Guidelines are to be welcomed. They incorporate the developments of the case-law since the entry into force of the VBER and, in so doing, they bring selective distribution into the new millennium, where online sales have come to occupy a much more important role. Suppliers will have more flexibility to draft the selective criteria applicable to online sales by authorised distributors, without having to worry about the currently applicable equivalence requirement between online and offline selective criteria.

In addition, the increased protection of authorised distributors against sales of the contract products by unauthorized distributors is to be welcomed. Authorised distributors often invest in a supplier's brand and are discouraged by sales by unauthorized distributors, leading to a potential unwillingness to keep up such investments. Moreover, the gradual rollout of selective distribution in the EU benefits SMEs.

To end on a note of caution, what is worrying is that the draft Vertical Guidelines, like they do in respect of non-selective distribution, foreshadow that the Commission intends to have more recourse to its possibility to withdraw the benefit of the VBER. For selective distribution, for example, the Commission mentions that the VBER is *likely* to be withdrawn where the products do not require selective distribution or the applied criteria, such as the requirement to have one or more brick-and-mortar shops. This is a worrying development in view of the safe harbour (and legal certainty) which a block exemption is supposed to offer the market participants.

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: Czech, Portuguese, Romanian, Slovak, Spanish, Swedish.

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