



Competition Law Update

September 2009

Proposed changes to the competition law rules governing supply and distribution agreements

The European Commission is currently revising the competition law regime applicable to agreements between parties operating at different levels of the supply chain. We examine the types of agreements which may give rise to a breach of competition law, the proposed changes to the current rules and the implications for your business.

The general rule

Agreements between parties operating at different levels of the supply chain may breach the general prohibition under competition law of anti-competitive agreements. This rule is not only applicable to formal or written agreements but extends to 'gentleman's agreements' and other forms of looser arrangements.

The penalties

The penalties which may arise in the context of any breaches of competition law can be severe, including fines and imprisonment. Also, the agreement giving rise to the breach may be unenforceable. As discussed elsewhere in this e-zine, anyone prejudiced by an anti-competitive practice can sue those responsible for damages and seek injunctive relief.

Types of agreement which may breach competition law

- *'Single branding agreements'* where a buyer is obliged or induced to concentrate his orders for a particular type of product with one supplier.
- *'Exclusive distribution agreements'* where a supplier agrees to sell products only to one distributor for resale in a particular territory. Generally, a distributor will also be limited in his reselling into other territories.
- *'Exclusive customer allocation agreements'* where a supplier agrees to sell his products only to one distributor for resale to a particular class of customers. Generally, a distributor will also be limited in his selling to other classes of customers.
- *'Selective distribution agreements'* which restrict the number of authorised distributors and the possibilities of resale, based on selection criteria linked to the nature of the product.
- *'Franchise agreements'* where one party grants to the other party the right to exploit a package of intellectual property rights (for example, trademarks, shop signs, know-how or patents) for the resale of goods or the provision of services to end users.
- *'Exclusive supply agreements'* where a supplier is obliged or induced to sell products only or mainly to one buyer.
- *'Upfront access payments'* which are fixed fees paid by suppliers to distributors in order to access their distribution network. This category includes fees paid by suppliers to retailers in order to obtain or retain access to their shelf space and payments to have access to a distributor's promotion campaigns.
- *'Tying'* which refers to situations where customers purchasing one product are required to also purchase another distinct product from the same supplier.
- *'Resale price restrictions'* include agreements which directly or indirectly establish a fixed or minimum resale price to be observed by the buyer.

Exceptions to the general rule

The parties to the above categories of agreement may be able to rely on certain exceptions to the competition law rules, primarily through the 'block exemption' process. The block exemption process involves evaluating an agreement by reference to a 'black list' which identifies the type of agreements which are not exempted from the prohibition of anti-competitive agreements. Therefore, if the block exemption does not prohibit something it is permitted.



The European Commission is currently reviewing the existing block exemption rules. The Commission has published a draft outline of proposed replacement rules and accompanying guidelines on their application.

Summary of proposed changes to the block exemption rules

Market share threshold:

Under the current rules, the market share of the supplier (where it sells the contract goods or services) must not exceed a 30% threshold in order to avail of the exemption. The market share of the buyer (where it resells the contract goods or services) is only relevant where an agreement obliges or induces a supplier to sell mainly to one buyer. In these circumstances, it is the market share of the buyer which must not exceed the 30% threshold.

The Commission has expressed concern at the increase in the market power of large distributors and retailers. To this end, it is proposed that under the revised rules the market share of the buyer, as well as the supplier, may not exceed 30% in order for the exemption to apply. Parties exceeding the 30% threshold would need to consider the application of certain other exceptions.

Resale price restrictions:

Currently, the Commission views all agreements which directly or indirectly involve the suppression of price competition with suspicion. The proposed new rules take a more nuanced approach to this issue, acknowledging that a fixed or minimum resale price may sometimes lead to efficiencies and benefit consumers. Under the new rules, it is contemplated that resale price restrictions may be permissible in certain circumstances, for example:

- Where a manufacturer introduces a new brand or enters a new market, such restrictions may provide the distributors with the means to increase promotional efforts, inducing them to expand overall demand for the product and making the entry a success.
- In franchise systems, fixed resale prices may be necessary to organise a coordinated short term (two to six weeks) low price campaign.
- Resale price restrictions may also be necessary to prevent a large distributor from using a particular brand as a loss leader, which could result in the delisting of that brand by other distributors.

Internet sales

Suppliers of branded goods often seek to impose restrictions on the territory into which, or the customers to whom, a buyer may sell the contract goods or services. Suppliers may wish to impose such restrictions in order to prevent sales through 'non-prestige' channels and to prevent sales into territories allocated to another buyer.

The current block exemption regulation distinguishes between restrictions on:

- "Active sales" in which a distributor actively approaches individual customers; and
- "Passive sales" in which a distributor responds to unsolicited demand from such customers.

Restrictions on active sales to territories or customers exclusively reserved to other distributors are generally permitted, however there must remain the possibility of passive sales. Under the current rules, every distributor must be free to use the internet to advertise or resell products and internet selling is not generally regarded as active selling.

The proposed new rules specifically identify certain types of restrictions on internet selling which may be problematic, for example, requiring distributors to:

- automatically reroute customers to the manufacturer or other distributor's websites;
- prevent customers located in another territory from viewing its website;
- limit the proportion of overall sales made over the internet; and
- pay a higher price for products intended to be resold by the distributor online than for products intended to be sold offline.



Competition law in recessionary times

As the downturn takes hold, businesses feeling the pinch may be tempted to de-prioritise their obligations under competition law. Has the Competition Authority adapted its approach to enforcement in these recessionary times?

Merger control approach

Commentators have broadly welcomed the Competition Authority's current pragmatic approach to merger control. When a transaction is notified to the Authority involving a business on the brink of insolvency, the Authority will examine the relevant competition law issues as a matter of priority. In the recent notification involving the purchase by HMV of Zavvi Ireland, the Authority accelerated its review timetable, halving the usual ten day notice period for the receipt of third party comments. In exceptional cases, when considering transactions involving insolvent or 'failing firms' the Authority may approve mergers which might otherwise be prohibited.

Anti-competitive practices approach

The Competition Authority's flexible approach to notified mergers should not be construed as a willingness to turn a blind eye to breaches of competition law. Notwithstanding the economic crisis, the Authority has indicated that it will be taking a tough line on businesses which engage in anti-competitive practices. The Authority has issued particularly stark warnings in relation to price fixing activity. The recent enforcement proceedings involving cartel activity in the car dealership and heating oil sectors have led to an increased awareness among businesses of the perils of price fixing.

Other cost saving activities which could breach competition law

However, many businesses are engaging in other forms of activity which could unwittingly land them in trouble with the Competition Authority. For example, businesses may collectively seek to negotiate better terms with suppliers through the medium of a joint purchasing group or trade association. The sharing or exchange of commercial information is another method used by smaller businesses to achieve parity with larger competitors.

There are significant competition law pitfalls associated with any form of cooperation between competitors. Even inadvertent breaches of competition law can give rise to significant penalties. When in doubt, businesses seeking to mitigate against financial pressures should seek legal advice.

Recent developments in the private enforcement of competition law

It has been reported that a number of candle manufacturers have initiated proceedings against Shell and Exxon Mobil, the alleged participants in a paraffin wax cartel. The candle manufacturers claim that they suffered losses arising out of alleged long standing agreements between the cartel participants to fix the price of wax. These proceedings come in the wake of the €676 million fine imposed by the Commission on those involved in the cartel. However, it should be noted that private enforcement is available even where national or European authorities have not taken enforcement proceedings.

This is the latest in a long line of ground breaking claims relating to breaches of competition law. Many claimants have accepted substantial out of court settlements. Moreover, European courts have increasingly demonstrated a willingness to grant injunctive relief to litigants, particularly where their livelihoods are at stake. The existence of economic evidence will be crucial in this regard.

New rules were introduced in 2005 with the aim of streamlining private enforcement proceedings before the Irish High Court. Under these rules, the judge may direct that the proceedings be adjourned to enable the parties to consider alternative methods of dispute resolution. This may prove to be faster and less cost intensive than proceeding to trial. Specialist judges with expertise in competition law are available to hear private enforcement actions and experts may also be appointed to assist the courts.

Beauchamps is well placed to assist parties who have been prejudiced by a breach of competition law, having recently achieved successful outcomes for clients involved in private actions.



Competition Authority: guidance on collective action in the pharmacy sector

In October 2008 the Competition Authority (the "Authority") consulted on collective action in the community pharmacy sector seeking input on ways in which health professionals, providing services for or on behalf of the State, might engage collectively with the Health Services Executive (HSE) in compliance with competition law. This is because competition law limits the coordinated activities of professionals like pharmacy contractors. On 23 September 2009 the Authority published its Notice in Respect of Collective Action in the Community Pharmacy Sector (notices set out the views of the Authority relating to a particular competition law area and are provided for guidance purposes only.)

The Notice gives guidance on the application of Irish and European competition law to collective action by community pharmacy contractors and other health professionals, when engaging with the HSE. In particular, it clarifies the limits competition law places on coordinated action by self-employed health professionals in relation to competitive factors such as fees.

The Notice restates the Authority's recommendation on the adoption of the "messenger model" for setting contractual terms and conditions. Provided adequate safeguards are put in place, this allows for a degree of collective input by self-employed health professionals while minimising the potential for collective action in breach of competition law. The messenger model would operate as follows. A third party (the "messenger") obtains from each service provider (e.g. each pharmacy contractor), individually, the level of fees that the service provider would require from the State to provide the relevant service. The messenger provides this information to the State, which uses it to devise a fee scale for the reimbursement of service providers that will secure the desired level of participation in the State's scheme. All communications between the messenger and individual service providers must remain confidential vis-à-vis other service providers, so that no service provider knows what any other service provider requires to participate. Each service provider would then be offered a revised contract by the State, which the provider, again individually, must choose to accept or reject. Under this model fees are not negotiated.

The Notice also takes account of the Financial Emergency Measures in the Public Interest Act 2009, the Minister for Health and Children's decision to alter remuneration of pharmacy contractors under this legislation from 1 July 2009 and the subsequent withdrawal of services by a number of pharmacies. It concludes that:

"widespread withdrawal by individual undertakings (pharmacies) following the decision of the buyer to fix a fee different from the fee recommended by the undertakings, in circumstances that are likely to give rise to a reasonable suspicion that the action is collective, might trigger an investigation by the Authority. In particular, an investigation would be more likely where there is widespread withdrawal at the national level, or where withdrawal was concentrated within a specific local market."

Beauchamps Solicitors advises the Irish Pharmacy Union ("IPU") on competition law issues. The issuance of this Notice is not a finding of wrong doing on the part of the IPU or its members.

Link to Notice

<https://www.tca.ie/templates/index.aspx?pageid=1272&locale=0>

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