

CPI's Europe Column Presents:

The state of debate – what to expect from the EU e-commerce sector inquiry

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When Michael Aldrich connected a modified TV to a computer via a telephone line, he invented the “Teleputer”, an early form of online transaction processing technique between consumers and businesses, which would later become known as e-commerce. It was 1979 in Hertfordshire, England. Mr Aldrich then spent the following decade campaigning to change the law in the U.K. to remove regulatory barriers for the use of his invention. Some 37 years later, the EU has become the largest e-commerce market in the world and the European Commission has launched one of its largest inquiries into the state of competition in the sector – the EU e-commerce sector inquiry.² After setting the scene on the current state of the debate, this article provides a summary of five likely outcomes of the inquiry.

Background: current state of debate

On 15 September 2016, the Commission published a Preliminary Report on the e-commerce sector inquiry, which it launched in May last year. The report is based on approximately 1800 submissions by manufacturers, retailers, marketplaces and copyright holders active in e-commerce. 8000 distribution contracts have been gathered by the Commission in the course of the exercise.

This inquiry takes place in the context of a wider EU initiative, the Commission’s Digital Single Market Strategy.³ This strategy has the ambitious target of creating a single market for online content and telecom services across the EU. The creation and protection of a single internal market within the EU is one of the overarching aims of the EU treaties and a particular quirk of EU competition law.⁴

To further promote and protect this ideal, the Commission is:

- developing a package of legislative measures with the aim of removing regulatory barriers to cross-border e-commerce⁵; and

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² European Commission, Sector inquiry into e-commerce, available at: http://ec.europa.eu/competition/antitrust/sector_inquiries_e_commerce.html (accessed on 1 November 2016).

³ European Commission, Digital Single Market online page, available at: https://ec.europa.eu/priorities/digital-single-market_en (accessed on 1 November 2016). See also European Commission, Press Release, “A Digital Single Market for Europe: Commission Sets Out 16 Initiatives to Make It Happen” available at: http://europa.eu/rapid/press-release_IP-15-4919_en.htm (accessed on 1 November 2016).

⁴ Article 3(3) Treaty on the EU provides that ‘The Union shall establish an internal market’ and Protocol 27 to the Treaty on the Functioning of the EU states that the internal market includes a ‘system ensuring that competition in the internal market is not distorted’.

⁵ A proposed regulation addressing geo-blocking is being considered by the European Council and Parliament, and is available here: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52016PC0289&from=EN>. Other legislative proposals include a directive on contracts for online and other distance selling of goods (available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015PC0635&from=EN>), a regulation on cooperation between national authorities responsible for the enforcement of consumer laws (available here: http://ec.europa.eu/consumers/consumer_rights/unfair-trade/docs/cpc-revision-proposal_en.pdf), a regulation on cross border parcel delivery (<https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-285-EN-F1-1.PDF>), an initiative to

- Through the sector inquiry, investigating barriers created by companies⁶.

The Commission uses the information obtained during a sector inquiry to understand the market better and decide whether and what action is required to address structural or behavioral competition concerns.

Although sector inquiries are not directed at investigating individual companies, they have often resulted in individual antitrust investigations for specific breaches of competition law uncovered during a sector inquiry.⁷ The Commission has reportedly already found some conduct through the e-commerce sector inquiry that it intends to investigate further. Competition Commissioner Margrethe Vestager has said that “the information gathered as part of our e-commerce sector inquiry confirms the indications that made us launch the inquiry” and “we need to take a closer look whether there is anti-competitive behaviour, which can be addressed by EU competition tools”.⁸

Enforcement action at EU level

The first outcome of the e-commerce sector inquiry is therefore likely to be more enforcement action at EU level against individual companies. However, rather than targeting straightforward cartels between competitors, the Commission intends to target conduct that is likely to fall in the “grey areas” of vertical restraints under EU competition law – i.e. arrangements between suppliers and distributors active at different levels of the supply chain.

For example, as regards the e-commerce in goods, the Preliminary Report has identified the following conduct as potentially problematic:

- Cross-border sales restrictions;⁹

modernise VAT on cross-border e-commerce (available at: http://ec.europa.eu/smart-regulation/roadmaps/docs/2016_taxud_002_iaa_vat_en.pdf), a regulation on cross-border portability of online content services in the internal market (available at: <http://ec.europa.eu/transparency/regdoc/rep/1/2015/EN/1-2015-627-EN-F1-1.PDF>), and a communications on the modernisation EU copyright (available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015DC0626&from=EN>). All links were accessed on 1 November 2016.

⁶ The Commission has the power to conduct investigations into sectors of the economy and into types of agreements where “the trend of trade between Member States, the rigidity of prices or other circumstances suggest that competition may be restricted or distorted within the common market.” (Article 17 Regulation 1/2003, available at: <http://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX%3A32003R0001>, accessed on 1 November 2016).

⁷ For example, when the Commission carried out a pharmaceuticals sector inquiry, the inquiry resulted in a number of individual enforcement actions in relation to patent settlements (“pay for delay”). In contrast, in another sector inquiry into business insurance, there was no subsequent enforcement action against individual companies.

⁸ European Commission press release, “Antitrust: e-commerce sector inquiry finds geo-blocking is widespread throughout EU”, available at: http://europa.eu/rapid/press-release_IP-16-922_en.htm (accessed on 1 November 2016).

⁹ 12% of respondent retailers reported that they have contractual cross-border sales restrictions in at least one product category in which they are active, by blocking access to websites, re-routing customers, refusing to deliver cross-border or refusing to accept cross-border payments. This conduct is likely to be problematic under EU competition law only in so far there is an “agreement” or “concerted practice” prohibiting cross-border active sales where there is no allocation of territory and/or unsolicited sales. Banning cross-border sales is permitted in selective distribution systems provided that supplier and distributor each has less than 30% of its respective market and cross-sales between members of the selective distribution system are not restricted.

- Restrictions on the use of marketplaces;¹⁰
- Restrictions on the use of price comparison tools;¹¹
- Pricing restrictions.¹²

The Commission has found that most of these restrictions affect the online sale of clothing and shoes, sports and outdoor, consumer electronics, cosmetics and healthcare, and home appliances.

As regards e-commerce in digital content, the Preliminary Report has identified the following conduct as potentially problematic:

- Restrictions in relation to transmission technologies, timing of releases and territories;¹³
- Long term exclusivity;¹⁴
- Geo-blocking;¹⁵

¹⁰ 18% of respondent retailers report that their agreements with suppliers contain marketplace restrictions. Whether marketplace restrictions not linked to qualitative criteria amount to hard-core restrictions under EU competition law is the subject of some debate and a German Court has referred the question to the Court of Justice (Case 230/16, Request for a preliminary ruling from the Oberlandesgericht Frankfurt am Main (Germany) lodged on 25 April 2016 — Coty Germany GmbH v Parfümerie Akzente GmbH, available at <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A62016CN0230>, accessed on 1 November 2016).

¹¹ 9% of respondent retailers reported that they have agreements with manufacturers which restrict their ability to use price comparison sites. Manufacturers often see these tools negatively because they focus solely on price. Amongst the potential concerns here, the Commission might consider that, in some circumstances, agreements restricting bidding behaviour in paid online search advertising may have harmful effects on competition. This may be particularly the case where one or more similar agreements include parties that collectively represent a material share of the relevant markets and, in the context of brand bidding restrictions, as a result of negative matching obligations in relation to brand terms which an advertiser would not negatively match but for the agreement.

¹² At least a third of retailers in each product category receive some form of price recommendations from manufacturers. Price recommendations and maximum recommended prices are not necessarily problematic under EU competition law, as long as they do not work in practice as minimum resale price maintenance (RPM) and the retailer remains free to set the price independently. The Preliminary Report states that certain pricing arrangements between manufacturers and their retailers may merit some further investigation.

¹³ 45% or more of the rights covered by the licensing agreements reviewed by the Commission are for the territory of one Member State only, release windows are contractually enforced and prevent distribution for a certain amount of time, and the transmission mode is often contractually proscribed. All of these features can mean that entry or expansion can prove difficult.

¹⁴ Licensing agreements are often in place for very long periods and are often renewed by the contracting parties. When the supplier and the distributor have high market shares (above 30%) and the exclusivity duration exceeds five years, these agreements can make entry and expansion difficult.

¹⁵ in order to limit the online transmission of digital content and to implement exclusive territorial licensing agreements, 70% of respondent digital content providers use geo-blocking measures (usually through IP addresses) to geographically restrict their content. Geo-blocking can be considered as another form of cross-border sale restriction and, as such, would only be problematic under EU competition law in so far there is an “agreement” or “concerted practice” geo-blocking digital content within the EU (See also European Commission staff working document “Geo-blocking practices in e-commerce - Issues paper presenting initial findings of the e-commerce sector inquiry conducted by the Directorate-General for Competition” available at: http://ec.europa.eu/competition/antitrust/ecommerce_swd_en.pdf, accessed on 1 November 2016). By

- Payment structures;¹⁶
- Other licensing structures.¹⁷

The Commission has already been active in its scrutiny of geo-blocking. It is still looking closely at video game makers and investigating whether their online distribution arrangements require further scrutiny.¹⁸

Enforcement action at national level

A second likely outcome of the sector inquiry is potentially the convergence of antitrust enforcement at national level. The Commission has consciously not prioritised cases on vertical restraints in the past 10 years, because the applicable rules (case law, Vertical Block Exemption Regulation and Guidelines¹⁹) have been relatively clear and straightforward. With the growth of e-commerce, however, questions on the interpretation of the rules have arisen within the European Competition Network (ECN)²⁰.

For example, online marketplaces have been at the forefront of debate across EU Member States and the Commission for some time. One question is whether absolute bans on the use of online marketplaces amount to hard-core restrictions in the form of restrictions of passive sales. A German Court has asked the Court of Justice of the EU for guidance on the legality of online platform bans in selective distribution systems²¹. The UK's Competition and Markets Authority (CMA) recently published an open letter to suppliers and retailers in which it said to have found the suppliers had illegally engaged in online RPM, specifying the minimum prices that the retailers could advertise for sales of the suppliers' products over the internet²², one

contrast, geo-blocking in the context of genuine agency arrangements or imposed unilaterally by a non-dominant company is unlikely to fall foul of EU competition law.

¹⁶ Although there is a variety of payment mechanisms under which providers can pay rights holders, the evidence gathered during the sector inquiry shows that the use of minimum guarantees and fixed/ flat fees are widespread, meaning that smaller entrants may have to pay the same amount as a large incumbent, which could make entry more difficult.

¹⁷ Licensing structures are complicated, and the way that online rights in digital content are split or bundled, and the stability and longevity of relationships between rights holders and providers mean that entry can be difficult.

¹⁸ Margrethe Vestager - Commissioner for Competition, "Competition policy for the Digital Single Market: Focus on e-commerce", Berlin, 26 March 2015, Speech at the Bundeskartellamt International Conference on Competition, available here: http://europa.eu/rapid/press-release_SPEECH-15-4704_en.htm (accessed on 1 November 2016).

¹⁹ The Vertical Block Exemption Regulation can be found at <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A32010R0330> and the related Guidelines are available at: http://ec.europa.eu/competition/antitrust/legislation/guidelines_vertical_en.pdf (accessed on 1 November 2016).

²⁰ The ECN is the mechanism through which the national competition authorities in all EU Member States cooperate with each other. See Commission Notice on cooperation within the Network of Competition Authorities, available at: [http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52004XC0427\(02\)](http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52004XC0427(02)) (accessed on 1 November 2016).

²¹ Case 230/16, Request for a preliminary ruling from the Oberlandesgericht Frankfurt am Main (Germany) lodged on 25 April 2016 — Coty Germany GmbH v Parfümerie Akzente GmbH, available at <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A62016CN0230>, accessed on 1 November 2016).

²² CMA, "Restricting resale prices: an open letter to suppliers and retailers", available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/530570/rpm-open-letter-suppliers-retailers.pdf (accessed on 1 November 2016).

of the restrictions looked at by the Commission in the Preliminary Report. The CMA's letter takes the opportunity to remind suppliers and retailers of the law on RPM, citing the imposition of substantial fines in two online cases where the CMA had found evidence of illegal RPM. Further, the CMA launched a market study into digital comparison tools (like price comparison websites and switching apps) on 29 September 2016²³. Although the CMA market study clearly overlaps with the scope of the e-commerce sector inquiry and, to some extent, risks creating duplication, the outcome of a CMA market study can be more far reaching than Commission sector inquiries in so far as the CMA could open a market investigation and impose behavioural or structural remedies if it found an adverse effect on competition resulting from certain features of the market, rather than from individual companies' conduct.²⁴

The results of the EU sector inquiry will provide useful factual background for an informed debate on e-commerce related issues within the ECN, possibly aimed towards achieving convergence and more coordination in national enforcement actions. For example, the EU pharmaceutical sector inquiry has largely achieved the goal of harmonising the way in which EU competition law authorities assess alleged "pay for delay" patent settlements across the EU – whether one agrees with the merits of such assessment or not.²⁵

Review of the existing rules

Thirdly, the results of the EU e-commerce sector inquiry will also be a catalyst for a debate on the EU Vertical Block Exemption Regulation and Guidelines in view of their ongoing evaluation. The Commission is keen to look at the legal framework on vertical restraints in light of current market realities. However, it does not want to immediately change the law or amend the Vertical Block Exemption Regulation or Guidelines, because while it is clear that the picture has changed since their last recast (in 2010), legal certainty remains important.

Facts and figures

Fourthly, the results of the sector inquiry will provide facts and figures which are likely to be useful background for the debates on legislative Commission initiatives relating to copyright (for example the proposed "portability regulation") and the proposed geo-blocking regulation.

As regards e-commerce in goods, the Preliminary Report makes the following observations.

- Price monitoring is widespread and often done by automatic software. Prices can change daily and even hourly, this is picked up instantly by other retailers and their

²³ CMA, "Digital comparison tools market study", <https://www.gov.uk/cma-cases/digital-comparison-tools-market-study> (accessed on 1 November 2016).

²⁴ CMA, Market studies and investigations - guidance on the CMA's approach: CMA3, available at: <https://www.gov.uk/government/publications/market-studies-and-market-investigations-supplemental-guidance-on-the-cmas-approach> (accessed on 1 November 2016).

²⁵ Appeals are currently pending before the General Court against the Commission pay for delay decisions and, similarly, an appeal is pending before the Competition Appeal Tribunal against the CMA first pay for delay decision.

own prices can be adjusted accordingly. “Is this perfect competition or perfect collusion?!”²⁶

- Manufacturers cite quality as being the main driver and pure online players cite price. This causes a tension which results in manufacturers opening their own online shops, creating dual distribution scenarios which potentially complicate the relationship with other online retailers.
- The Commission has reviewed thousands of agreements. It has identified various types of restraints which it regards as problematic – e.g. pricing limitations and recommendations and cross-border sales restrictions on active sales even where there is no allocation of territory. The Commission staff expressed some concern and surprise at this as it perceives that the Vertical Block Exemption Regulation makes it clear that RPM and the prohibition of cross-border active sales where there is no allocation of territory and/or unsolicited sales constitute hardcore restrictions of competition.²⁷

As regards e-commerce in digital content, the Preliminary Report further notes the following.

- Transmission rights are often licensed on an exclusive basis, often territorially, and not available on a standalone basis. All of these factors make it difficult for smaller or new entrants.
- Digital markets are all idiosyncratic and very different from another, and need to be looked at on their own terms/ market realities (i.e. satellite TV, cable, mobile, digital).
- Digital markets also seem still to be using conservative, up front, fixed price models and haven't changed with the markets/ new technologies.

Action for businesses

Last but not least, the e-commerce sector inquiry provides the opportunity for companies to review/audit existing contractual relationships and if necessary bring distribution contracts into line with EU competition law. The Commission has specifically advised companies to do so - Margrethe Vestager said that “it’s up to businesses to make sure their contracts don’t harm competition online” and advised “every business that’s involved with e-commerce” to check that they’re complying with the rules²⁸. Such a clear message should make it is easier for in-house lawyers to convince management that such a review/audit is necessary and worthwhile. Getting it wrong could have serious consequences, including the risk of:

²⁶ Thomas Kramler (DG Competition, European Commission), “E-commerce sector inquiry”, presentation held in Brussels, on 13 October 2016.

²⁷ *Ibid.*

²⁸ Speech, “E-commerce: a fair deal for consumers online”, Stakeholder Conference on Preliminary Findings of the E-commerce Sector Inquiry, Brussels, 6 October 2016, available at http://ec.europa.eu/commission/2014-2019/vestager/announcements/e-commerce-fair-deal-consumers-online_en (accessed on 1 November 2016).

- expensive investigations and disruptive on-site inspections;
- distraction of management resources from ordinary business to having to deal with extensive information requests from the antitrust authorities;
- hefty fines in case of finding of infringement; and
- actions for damages from customers who have suffered a loss as a result of the infringing conduct.

Next steps

The Commission is now inviting a public consultation on its preliminary report for 2 months until 18 November. Its final report is due in the first quarter of 2017. Overall, the e-commerce sector inquiry is a useful exercise and the Preliminary Report is a comprehensive and informative document that should provide useful background facts, spur the discussion on how to approach restrictions of competition in e-commerce in the EU, and allow for informed policy making in the future. The debate on the removal of barriers to e-commerce, started by Aldrich's first online shopping system some 37 years ago, seems far from being over.