

Selective distribution systems: AG Wahl advises to allow a ban on sales via online marketplaces

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In his opinion in *Coty*,¹ Advocate General (“AG”) Wahl invites the European Court of Justice (“ECJ”) to rule that a manufacturer operating a selective distribution system is, under certain conditions, **allowed to prohibit its authorised retailers from selling the products online via third-party platforms**.

The opinion also offers a **strong endorsement of selective distribution systems** and confirms that, as long as certain conditions are met, these systems **do not infringe Article 101** of the Treaty on the Functioning of the European Union (“TFEU”).

If the ECJ follows AG Wahl on all points, manufacturers of luxury products will be able to keep a tight grip over their selective distribution networks in the EU. It remains to be seen what impact this will have on online platforms, as this will depend in large part on the details and possible nuances in the ECJ’s decision. Of course, the ECJ is not bound by AG opinions and may reach different conclusions in its judgment, which should normally be expected towards the end of this year.

A. Background

Coty is a manufacturer of luxury cosmetics, which distributes its products through a selective distribution network of authorised retailers that are required to meet a number of qualitative requirements. Coty allows the resellers to sell the luxury products on the internet through an “electronic shop window” on the condition that the products’ luxury character is preserved. At the same time, Coty generally prohibits its resellers from engaging third-party online resellers that are “discernible to the public to handle internet sales” (e.g. eBay or Amazon). The prohibition is imposed irrespective of whether the third-party online reseller respects the manufacturer’s quality standards, which would apply to the reseller’s own webpage.

One reseller refused to adhere to this prohibition and began selling Coty’s goods on amazon.de. Coty sought to enjoin the reseller from doing so, but the lower instance court refused to enforce the restriction, finding that it violated both EU and German competition law.² On appeal, the Frankfurt Higher Regional Court sought a preliminary ruling from the ECJ to determine basically: (a) whether selective distribution systems that aim to distribute luxury goods while ensuring a “luxury image” are in general compatible with Article 101 TFEU and (b) whether the prohibition of third-party online sales is compatible with the applicable EU competition law.

The ECJ’s judgment is expected to clarify a number of important questions and to shed light on the implications of the ECJ judgment in *Pierre Fabre*,³ which was relatively strict and prompted some commentators to doubt altogether the legality of selective distribution systems for luxury goods. The matter in question is also quite contentious in Europe, with national competition authorities and courts reaching conflicting decisions. The German competition authority, in particular, has emerged as a staunch supporter of the proposition that selective distribution systems cannot restrict the resale of products online via third-party platforms. The broader importance of the case is explained by the number of governments intervening.

¹ Case C-230/16 *Coty Germany*.

² The lower court relied on Case C-439/09 *Pierre Fabre Dermo-Cosmétique SAS*.

³ See ECJ Judgment of 13 October 2011 in case C-439/09 *Pierre Fabre Dermo-Cosmétique*.

Germany and Luxembourg, in their observations, took the position that such restrictions are anti-competitive, while France, Italy, Netherlands, Austria and Sweden favoured allowing restrictions on selling on online marketplaces. The European Commission (“**Commission**”), in its observations, also unequivocally endorsed the latter approach, which is consistent with its Vertical Guidelines and its statements in the context of its recent E-commerce sector inquiry.

B. Strong endorsement of selective distribution systems

AG Wahl first clarifies the much-debated potential contradiction between the older case law on selective distribution systems (the well-known *Metro* case)⁴ and the ECJ judgment in *Pierre Fabre*. The AG reaffirms the continued pertinence of the older case law by reconfirming that, under certain criteria,⁵ **selective distribution systems** that have as their aim the distribution of luxury goods, and primarily serve to preserve the “luxury image” of those products, **are compatible with Article 101(1) TFEU**.

In line with his opinions in other cases, the AG **employs an economic approach** and stresses the positive (or at least neutral) economic effects of selective distribution systems. The AG goes as far as to observe that manufacturers will end up “auto-regulating” the scope and strictness of their selective distribution systems to optimise economic efficiency, as otherwise they would lose market share and customers.⁶ The AG also underscores that EU competition law does not consider price competition as the only possible or even the most efficient model of competition, but that it also **assigns an important place to competition on qualitative aspects**. He views this as another argument for the legitimacy of selective distribution systems and considers that all aspects of competition should be taken into account when determining an agreement’s impact on competition. Then, the AG also notes that the fact that selective distribution systems might result in an imbalance of power between the contractual parties should be irrelevant for the purposes of competition law.⁷

AG Wahl also observes that, in determining whether a selective distribution system complies with the required conditions, the **intrinsic properties of the products are less important** than the company’s assessment that the selective distribution system is necessary for a proper functioning of its distribution network, with a view to preserving the image of the brand or the quality of the products.⁸ This view appears to be extending the legality of selective distribution systems beyond the mere scope of luxury products and it will be interesting to see if the ECJ follows the AG on this point. The next battle before the national courts might be on the question of whether specific goods that a manufacturer decides to distribute through a selective distribution system qualify under the relevant criteria for distribution in such a manner.

C. Prohibition of sales on online marketplaces

Against that background, the AG examines whether there is an objective justification for the **prohibition of sales on online marketplaces** that Coty imposed on its resellers. In that regard, he reasons that a prohibition of online sales through third-party platforms is comparable to quality requirements that a manufacturer can legitimately impose on its resellers for their brick-and-mortar shops as well as for their online sales.⁹ AG Wahl takes the view that such a prohibition is **legitimate and proportionate** since the manufacturer has a legitimate aim of ensuring control over the distribution of its products, whereas such control would be impossible over a third party’s online platforms. Such a prohibition is also likely to improve competition based on qualitative criteria, as it is likely to protect the luxury image of the products and to safeguard against freeriding by other companies.

Notably, in AG Wahl’s opinion, a ban on online marketplaces would still be legitimate even if third parties established **luxurious, specifically-branded “shop-in-shop” subpages**, as such subpages would still not be under the manufacturer’s control. Should the ECJ espouse the AG’s view on this point, this could mean a considerable obstacle for online platforms in doing business with members of selective distribution systems.

⁴ See Case 26/76 *Metro SB-Großmärkte v Commission*.

⁵ The criteria that have been established previously and that the AG’s opinion reconfirms are: (1) the resellers are chosen on the basis of objective criteria of a qualitative nature, which are determined uniformly for all and applied in a non-discriminatory manner for all potential resellers; (2) the nature of the product in question, including the prestige image, requires selective distribution in order to preserve the quality of the product and to ensure that it is correctly used; and (3) the criteria established do not go beyond what is necessary.

⁶ AG Wahl Opinion, para. 44.

⁷ AG Wahl Opinion, para. 48.

⁸ AG Wahl Opinion, para. 46.

⁹ European Commission Guidelines on Vertical Restraints (2010/C 130/01), para. 54.

The opinion concludes that the **prohibition in question would not fall within the scope of Article 101(1)** if it fulfils the conditions that generally apply to selective distribution systems more broadly.¹⁰

The AG also distinguishes the limited scope of the prohibition of certain forms of online sales in *Coty* from the outright and complete prohibition of all online sales, as seen in *Pierre Fabre*. Notably, *Coty* did not prevent its resellers from making online **sales through their own webpages**. AG Wahl's conclusions in *Coty* are also limited to the **use of third-party platforms "in a discernible manner"** and nothing in the opinion precludes the resellers from using third-party platforms in a non-discernible manner. The opinion does not explain the meaning of "non-discernible" but it might be interpreted as using webpages that do not include any references to a third party, such as logos. Similarly, an agreement with a market platform to direct customers' searches to the reseller's webpage is unlikely to be seen as "discernible"; this should allow resellers to continue selling the products via the platforms.

AG Wahl further stresses that the prohibition in question could not be interpreted as a substantial restriction of online sales, because the third-party platforms are still a relatively marginal method of selling products online.¹¹ He acknowledges, though, that this **might change in the "more or less long term"**. AG Wahl refers to the Commission's findings in the E-commerce sector inquiry that was concluded in May 2017. The Commission's final report establishes that restrictions on the use of marketplaces are **mostly found in selective distribution agreements** and that they typically concern branded goods, but interestingly are not limited to luxury, complex or technical goods.¹² In this report, the Commission reached similar findings as AG Wahl regarding the effect and legality of prohibition of third-party online sales.¹³

Finally, AG Wahl examines what would happen if the prohibition in question **fails to fulfil the required conditions** and thus is found to fall under Article 101(1) TFEU.¹⁴ He concludes that the prohibition could still be **justified by the application of Article 101(3) TFEU**, either through the application of the block exemption provided for in Regulation 330/2010¹⁵ or on the basis of a case-by-case individual analysis. He sees **no reasons for such prohibition to be treated as a restriction "by object" under Article 101(1) or as a "hardcore restriction" in the sense of the block exemption regulation**. AG Wahl clarifies that the ban on sales via online marketplaces **should not be seen as a restriction on passive sales** and thus discredits the idea that all internet sales are to be considered passive sales. This leads to the conclusion that such prohibitions could be block exempted (if the market share safe havens of Regulation 330/2010 are not exceeded) and, therefore, **presumed to be legal**.

¹⁰ See footnote 54 above.

¹¹ It is noteworthy that, while the Commission's report in general confirmed that third-party platforms are still relatively marginal in the EU, it has reached a different conclusion for the German national market, where 62% of the respondents to the Commission's sector inquiry used marketplaces.

¹² Commission's Final report on the E-commerce Sector Inquiry, 10 May 2017, para. 40.

¹³ Commission's Final report on the E-commerce Sector Inquiry, 10 May 2017, paras 41-42.

¹⁴ AG Wahl argues that this could only be concluded through a **"by effect" analysis** and never by resorting to the stricter "by object" analysis.

¹⁵ Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the TFEU to categories of vertical agreements and concerted practices (OJ L 103).

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