E U R O P E A N E C O N O M I C A R E A

S T A N D I N G C O M M I T T E E
O F T H E E F T A S T A T E S

1/MP/W/002
31 July 1997
Brussels

WORKING GROUP ON COMPETITION POLICY

Comments by the EFTA Working Group on the Commission Green Paper on Vertical Restraints in EC Competition Policy

I INTRODUCTION

1. The EEA/EFTA States welcome the Green Paper on vertical restraints. The Commission has taken a broad and in-depth approach to the revision of the present framework, both legally and economically. Transforming the findings of economic theory into general and legally binding rules is an extremely difficult and challenging task. In this respect, the Green Paper represents a broad and workable basis for further discussion.

2. The main goal of competition law is to promote the efficient use of the society's resources by means of workable competition. Workable competition may only be achieved where an agreement's potential negative impact on competition is outweighed by positive elements, such as innovations or increased inter-brand competition. The legal framework should therefore accept innovative solutions, leaving the parties free to try out and exploit new distribution systems and agreements. Flexibility with regard to the parties' freedom of choice must with this background be considered as one of the key instruments to promote workable competition. The legislation must, however, ensure that all harmful restrictions of competition are eliminated. With a view to promoting innovations, this is best taken care of by focusing on the economic impact of the agreement in question.

3. The EEA/EFTA States have examined the issues of legal and economic nature mentioned in the Green Paper and the Rey/Caballero study. In Norway a national hearing has been arranged.

II ECONOMIC BACKGROUND

4. Economic theory has shown that no safe conclusions can be drawn as to whether vertical restraints have a positive or negative effect on competition. Such restraints should therefore be considered on a case-by-case basis, as their impact on the relevant market will vary considerably, depending on factors such as the market structure, the degree of concentration, the existence of parallel networks etc.

5. The conclusions of the EEA/EFTA States on the analysis of the economic impact of vertical restraints are mainly coherent with the ones laid down in the Green Paper and the Caballero/Rey study. This is in particular the case in relation to the fact that vertical restraints may facilitate market entry and lead to efficiency gains in distribution. Vertical restraints may, however, also be harmful to competition, e.g. by increasing the importance of barriers to entry.

6. With regard to specific restrictions, some comments on RPM and total territorial protection should be added. The EEA/EFTA States agree that the impact of RPM in most cases is negative. In this respect, however, a distinction should be made between price floors and price ceilings. The introduction of price ceilings could prevent abuse of local market power within an exclusive area, or eliminate double-marginalisation problems. On the other hand, price floors will rarely have a positive impact on competition. The restraint should not, however, be excluded from possible exemption on an individual basis: in certain cases it may be a tool in penetrating new markets.

7. As for total territorial protection, the EEA/EFTA States would like to point out that the existence of such restraints in certain cases may promote integration. This is due to the fact that the possibility of granting a retailer total territorial protection may increase the incentive to be present in more markets. For instance, if price differentiation is possible, a producer will be able to export to low-price countries. It must be considered doubtful whether he will do this if he fears meeting price-competition on his home-market from re-imported goods. It follows that territorial protection in fact may promote market-integration by means of increased inter-brand competition. Territorial protection may also be useful in eliminating free-riding, which again may promote pre-sale service.

8. The EEA/EFTA States agree that a general exemption for these traditionally hard-core restrictions should not be granted. A presumption that individual exemption should never be possible, however, does not seem to comply with the findings of economic theory.

III COMMENTS ON THE FACT-FINDING

9. The EEA/EFTA States can confirm the findings of the Commission. However, some comments with regard to the development of discount-systems with possible foreclosure effects, e.g. so-called loyalty cards should be added. This has not been examined in the Green Paper.

10. The EEA/EFTA States and, in particular Norway, have identified an increasing number of such cards, especially in the sector of groceries and consumer-related markets. The use of such cards may have a negative impact on competition, by reducing market transparency on relative prices and increasing consumers loyalty to specific suppliers. Loyalty cards may provide incumbent suppliers with important information

about consumers' preferences. The result may increase interdependence between producers and retailers, making it difficult for new suppliers to enter the market.

11. Clauses making the use of a specific loyalty card mandatory should therefore be addressed explicitly in future block exemptions or negative clearance regulations. It can be argued that the actual clause does not merit a general exemption, due to the above-mentioned impact on competition. The obligation should at least be limited to a specific period of time.

12. The EEA/EFTA States would also like to focus on the increasing degree of concentration, especially on the retail level. The existence of chains should be explicitly addressed in the new rules governing vertical restraints. This may in particular be important in connection with loyalty cards, as agreements introducing such systems in most cases are negotiated between groups of retailers or franchisers. In this respect, the EEA/EFTA States support the proposal in Option II that associations of independent retailers could benefit from block exemptions.

IV EXPERIENCE WITH THE PRESENT LEGAL FRAMEWORK

13. The EEA/EFTA States agree that the present rules do have a straitjacket effect, and that this should, to the extent possible, be avoided in future regulations. The straitjacket effect relates mainly to two different issues; on the one hand, that the contracting parties are limited in their freedom to choose flexible solutions and to adopt a contract individually adapted for them; on the other hand the innovation of new distribution systems is slowed down. However, the present legal framework provides for a high degree of legal certainty, the importance of which should not be underestimated.

14. Small undertakings without in-house lawyers often have problems adapting to the legislation. In this respect, it should be pointed out that the regulations are often worded in such a way that they are not immediately accessible to undertakings without legal expertise.

15. The present system leads to a high number of notifications, also in cases where an individual assessment would not be necessary. This is a burden for private parties, in particular for small undertakings with limited resources. Concerning the Commission's need for information, other solutions to respond to this need should be considered. Reducing costly notification procedures is, in any case, a matter of importance.

16. One problem which occurs for all notifying undertakings is the extensive time of case-handling. This issue has been resolved under the Merger Regulation by means of imposing legally binding time-limits on the Commission. In this respect attention is also drawn to the fact that it is expensive to make use of the non-opposition procedure, compared with the benefits that may be achieved.

17. Finally, the Commission notices may in certain cases create legal uncertainty. This would in particular seem to be the case with the Notice on co-operation between

undertakings and the Court of Justice's interpretation of the *de minimis* doctrine compared to the Commission's approach. As for further experiences with current legislation, the EEA/EFTA States adhere to the conclusions in Chapter VII of the Green Paper.

V REGULATIONS OR NOTICES?

18. The balancing of flexibility and a workable degree of legal certainty must be the main goal when drafting a new legal framework in the field of vertical agreements. Experience has shown, however, that it is difficult to draft binding regulations providing for exemptions from the prohibition in Article 85(1) in such a way. Thus, it must be considered whether the aim is reached more effectively by means of other kinds of legal acts, or if the drafting of the regulations can be improved.

19. With regard to the legal form of new provisions, the current options are Commission notices or regulations. Notices are not legally binding, and may be overruled by the Court of Justice. Notices are also drafted in rather general terms, and are thus not precise as to what is covered. Binding regulations must generally be considered to provide for a higher degree of legal certainty than notices.

20. Rules given as notices under Article 85(1) must be deemed to increase the number of notifications, as legal certainty is aimed at by most undertakings. As companies in the EEA/EFTA States in general are rather small, it is not likely that the number of notifications to the EFTA Surveillance Authority would increase significantly. Soft-law under Article 85(1) may lead to the divergent application of the Article, considering the increasing number of cases involving national authorities and courts. If legislation were issued under Article 85(1), binding regulations would therefore seem necessary.

21. Notices issued under Article 85(1) would arguably give more extended competence for national authorities to apply national competition law than regulations under Article 85(3), provided that the principle of primacy of community law applies to block exemptions. It should be noted, however, that national law can always, whether or not the principle of primacy applies, be applied to the extent that an agreement is not caught by Article 85(1), and even if the agreement in question is covered by a block exemption regulation. On the other hand, if block exemption regulations are drafted more extensively than what is strictly required by Article 85(1), this could hinder the application of national law, thus rendering the control of the markets less effective.

VI BASIC ASSESSMENT OF THE OPTIONS

22. The options set out in the Green Paper points 281 – 301 imply to some extent a choice of fundamental nature between different systems and approaches of antitrust law. While the present system, based on general prohibition, remains in force under options I – III, option IV introduces a kind of abuse-control system, as most vertical agreements

are declared to be *a priori* legal, and subject to individual assessment under a refutable negative clearance regulation.

23. The EEA/EFTA States believe that a system as outlined in Option IV may solve some of the major shortcomings of the present system. Option IV puts forward interesting opportunities, both with regard to flexibility and the legal certainty for private parties. A situation where most vertical restraints are deemed not to be caught by the prohibition in Article 85(1), thus rendering burdensome notification procedures unnecessary, would certainly increase legal certainty and facilitate the enforcement of the law. Furthermore, we are of the opinion that a narrow interpretation of Article 85(1) is more in line with the case-law of the Court of Justice and economic theory than the rather broad approach taken by the Commission. In line with the above, a system under Art. 85(1) should be based on regulations and not on non-binding notices.

24. However, the introduction of such a system would require an in-depth analysis with regard to the compatibility with the EC-Treaty, in particular the competence of the Commission in relation to the Court of Justice in interpreting Art. 85(1).

25. Article 85(1) is a provision built on the principle of prohibition; however, it requires an individual assessment of the agreement or concerted practice in question. No agreement or concerted practice is therefore in principle *a priori* legal or illegal. This also applies of course to vertical agreements.

26. A legal situation in which most vertical restraints generally are declared to be *a priori* legal, would thus probably not be compatible with Article 85(1). As the Article requires an individual assessment, the application of a negative clearance regulation would at least have to be differentiated following suitable criterion with regard to the negative impact of the agreement. Such a solution would, however, not eliminate the need for notification in cases which raise doubt as to whether the agreement is covered by the regulation or not.

27. The substantive law of Article 85(1) is laid down by the Treaty and further developed by the Court of Justice and the Court of First Instance. Anybody with a sufficient legal interest in the case can challenge or defend the validity of an agreement before a national court. As the prohibition is directly applicable and the provisions of a negative clearance regulation will have to be drafted within its confines, Option IV would, as for the substantive law, not seem to entail any amendments at all.

28. Experience has shown, however, that private parties under the present system lack procedural instruments to establish whether an agreement is caught by the prohibition or not. The lack of case-law on the correct interpretation of the prohibition has, in this respect, led to a situation with a low degree of legal certainty under Article 85(1). If Option IV can establish such instruments, it is welcomed. In this respect, attention is drawn to the fact that block exemptions under Article 85(3) may reduce the incentives to challenge agreements under Article 85(1), thus hindering a correct interpretation being developed by the Court of Justice and the Court of First Instance in their case-law.

29. The EEA/EFTA States stress the importance of a further analysis of the legal questions arising from Option IV. They will await taking a final position with regard to the various options put forward in the Green Paper on the legal framework until these matters have been clarified. In the meantime, EFTA comments are based on the present legal framework, i.e. a system with block exemptions or Commission notices. Certain aspects of Option IV will, however, be examined and some of the proposed amendments to the substantive law may also be carried out within the confines of a negative clearance regulation.

VII PROPOSED PROCEDURAL AMENDMENTS

30. The general impression is that the present procedures for notification are too burdensome and complex to effectively provide for legal certainty. It has been pointed out that the Commission's capacity problems make it difficult to have fruitful pre-notification contacts. It seems, however, that procedures of a rather complex nature are needed to provide for a satisfactory degree of legal certainty and to enable the undertakings to make use of their rights to be heard and to have access to the file. This is especially the case with the withdrawal of the benefits of a block exemption.

31. Rather than amending the procedures, it would seem useful to decrease the number of agreements that need notification. This could be done either by exception of more agreements from the obligation to notify, or by extending the scope of the block exemptions. With a view to promoting legal certainty, it is doubtful whether extending the scope of Article 4 of Regulation 17 is the appropriate approach, as procedural amendments do not influence the state of the substantive law under Article 85(1). Extending the scope of the block exemptions does therefore seem to be a more realistic approach. To the extent that one chooses to except more agreements from the obligation to notify, the legal status of such agreements should be clarified.

32. As indicated above, the present non-opposition procedure is often regarded as too complicated and costly compared to the benefits that can be achieved. There seem to be two ways of promoting and extending the use of this procedure: increasing the benefits or facilitating notification.

33. Concerning the first option, the procedure could be extended to cover whole agreements, as opposed to the present system, in which only single clauses are covered.[1] Furthermore, with a view to reducing the mass-problem, national competition authorities could be involved in the case-handling on a more extensive basis, e.g. by providing information about relevant markets, the undertakings concerned, etc. With the

---

[1] The non-opposition procedure could be modelled on the present Regulation 417/85, (exempting categories of specialisation agreements), where the procedure covers the whole agreement.

situation at present, opposition should generally only be raised on a request from national authorities.

34. Concerning the second option, to facilitate notification or case-handling, the question could be raised whether a simplified non-opposition procedure complies with Article 85(3) and the requirements set forth in Regulation 17 and Regulation 19/65. This question should be further examined. It should be noted, however, that an exemption by decision or non-opposition cannot be granted unless the procedures laid down in Regulation 17 are followed, as it has already been questioned whether the existing non-opposition procedures are *ultra vires*. As amendments to Regulation 17 will undoubtedly increase the period of time required for issuing new regulations, this option will not be considered further in the present paper.

35. A procedure similar to the existing non-opposition procedures should, however, in any case be introduced in all block exemptions, with an opposition period of four months.[2]

36. At present, a single clause that is not covered by the exemption can render null and void all contractual provisions that are contrary to Article 85(1). This seems to be a somewhat strong reaction, taking into consideration cases where the parties have misunderstood the block exemption or interpreted it incorrectly. The Commission retains the possibility to fine undertakings for infringements of Article 85(1). It does not, therefore, seem necessary to uphold the present state of the law, and a rule providing for severability for the remaining parts of the agreement should be introduced. Single clauses not covered by exemption should, of course, continue to be null and void to the extent that they are infringements of Article 85(1).

37. The introduction of an arbitration procedure for refusals to deal under selective distribution systems does not seem appropriate. These problems may be resolved under the present rules, by means of procedures before the Commission or national courts.

VIII PROPOSED SUBSTANTIVE AMENDMENTS

38. Economic theory concludes that a case-by-case analysis is required for the assessment of vertical restraints. It follows, however, from the Green Paper that this task is beyond the capacity of the Commission. This requires general parameters of an economic kind to be included in the legal framework.

39. The EEA/EFTA States have examined whether market-shares should be used as a criterion for the application of block exemption regulations. It should first be pointed out that according to economic theory, market-shares are not the only criterion that can indicate whether a vertical restraint is harmful or not, nor is it in many cases the most realistic criterion. Economic theory considers indicators such as the degree of concentration on the relevant market, the degree of market-integration, the development

---

[2] Cf. Regulation 240/96, exempting categories of technology transfer agreements.

of market-shares over a certain period of time and the cumulative effect of parallel networks as being relevant. The main problem with these indicators is that they are in practice even more difficult to determine than the parties' own market-shares.

40. The introduction of market-shares has in particular been contested with the argument of legal certainty. In the EEA/EFTA States' view, this problem can be avoided by fixing the limit at a reasonably high level. It must be presumed that undertakings of a certain size are aware of their market position, and their shares of the total turnover. A high level would also, from a statistical viewpoint, reduce the number of cases involving doubt. Flexible instruments must be introduced in order to increase the legal certainty for undertakings with "critical" shares.[3] Legal certainty could also be established by means of an opposition procedure. Guidelines in this regard should be issued.[4]

41. As for the definition of the relevant market, this is already provided for in the forthcoming Commission Notice. It should, however, be specified on which level the market shares are to be assessed, i.e. on the retail, wholesale or production level. In the EEA/EFTA States' view, the most realistic approach seems to be to use the level on which the share is the highest. Market-shares should be based on actual sales and assessed *ex ante.*

42. It should be noted that a market-share exceeding the limit should not lead to the non-application of the exemption. Instead, exceeding the market-share limit should trigger the application of an extended black-list, or the application of further conditions (cf. point 51 seq. below). As an alternative to market-shares, the opportunity to withdraw the benefits of the exemption should be facilitated. National authorities may be involved to a greater extent in this procedure.

43. The scope of the existing regulation should be extended. It seems, however, that the main categories of exemptions, i.e. exclusive dealing and franchising, can be upheld. The question of cumulative application should be clarified, preferably by way of a notice. It does not seem necessary to issue a regulation for selective distribution systems, as such arrangements seem either to be covered by Article 85(1) and not to be exempted, or they are not infringements of the prohibition.

44. Firstly, the existing regulations should be extended to cover services and goods for processing. The EEA/EFTA States do not consider that the negative impacts in the relevant market are more harmful for such agreements than for agreements limited to goods for resale. It should also be noted that the required benefits, i.e. consumer benefits and efficiency gains in distribution, must be deemed to be obtained by agreements extending to services or goods for processing. The distinction between goods for resale and services and/or goods for processing is difficult to determine. In this respect, weight should also be attached to the fact that vertical restraints extending to goods for

---

3 A mechanism modelled on Regulation 417/85 and 418/85 could be introduced in this respect.

4 Table II in the Green Paper could be incorporated in such guidelines.

processing would facilitate export of raw materials and semi-manufactured articles, which will increase efficiency.

45. Furthermore, the existing regulations should be extended to cover multilateral agreements. This is in particular important for franchise agreements. However, weight should be attached to the fact that such amendments require a new enabling regulation from the Council, which would extend the period before new regulations could enter into force. Such an extension would, however, significantly facilitate the drafting of franchise agreements.

46. The block exemption for exclusive purchasing agreements should be extended to cover less than 100 % exclusivity. It does not seem to be reasonable to uphold a condition of total exclusivity.

47. As for the drafting of new block exemption regulations, the EEA/EFTA States consider that the approach should be changed from clause-specific to more impact-orientated. This may to a certain extent reduce the legal certainty compared to the present regulations, but it is submitted that this effect probably will be outweighed by efficiency gains.

48. At present, all inherent restrictions of an agreement covered by the scope of application of a block exemption are automatically exempted. To obtain a greater flexibility, this general and automatic exemption could be extended to all *ancillary restraints*, i.e. additional restraints that are necessary with regard to the main agreement and with only insignificant effect on competition. Such an extension must be deemed to be within the powers of the Commission under Article 85(3) and Regulation 19/65 Article 1.

49. Most of the straitjacket effect can be traced back to the white-list. After what has been said above about flexibility, it does not seem appropriate to uphold the present technique of white-listing specific clauses. The EEA/EFTA States suggest that the white-lists in the future lay down specific purposes that can be obtained within certain fields. Within these fields, all necessary and proportional clauses should be automatically exempted. This criterion should be well suited for application by national courts.

50. These fields and “legal purposes” must however, not be defined too broadly, but be specific in nature in order to prevent abuse. For example, Article 3 of the Franchise Regulation could have been limited to define the scope of exempted clauses, i.e. clauses necessary to maintain the common identity and reputation of the franchised network. Which specific clauses that are chosen for these purposes should be left at the discretion of the parties, a solution that certainly would promote innovations in distribution systems.

51. This approach may in certain cases lead to an appreciable restriction of competition that would not be exempted under Article 85(3). The respective regulations should therefore also contain specific conditions, which must be satisfied in order for

the agreement to benefit from the exemption, thus ensuring that workable competition is maintained on the relevant market. In addition, time-limits should be laid down.

52. An alternative may be to extend the black-lists. This extended black-list should, however, only apply to agreements where *one party's* market-share exceeds a certain limit. It should be sought to avoid laying down black clauses where the same goals can be achieved by conditions for the application of the regulation, e.g. that instead of black-listing prohibitions of passive sale, stipulating a condition that customers always have alternative retailers.

53. Even though the regulations are drafted in such a way as to contain rules implying discretion, it should be pointed out that these may be applied and construed by national courts or administrative authorities, thus enabling the parties to the agreement to obtain legal certainty. It should also be pointed out that involving national courts to a greater extent would contribute to focusing on competition law and issues. It should also be considered that the national authorities may play a more active role, in particular with a view to withdrawal of the benefits of an exemption.

54. The block exemptions should thus be restructured in the following manner. A clear definition of the agreement exempted, followed by a clear provision that ancillary restraints are exempted automatically. The regulations should also contain a "white-list", laying down purposes that could be achieved by necessary clauses and the fields within which such clauses are accepted. Finally, provisions governing conditions and a black-list applying in cases involving undertakings with high market-shares should be included.

IX CONCLUDING REMARKS ON THE OPTIONS

9.1 Option I

55. The above has shown that the present legal framework needs revision. This option can thus not be recommended.

9.2 Option II

56. Most of the proposals set out in Option II seem to be workable tools for improving the legal framework. The proposal to include price ceilings in the franchise block exemption is welcome. However, such price ceilings should also apply to the other regulations.

57. Furthermore, it seems reasonable to extend the existing regulations to cover agreements between more than two parties. An exemption can also be issued for co-operation within groups of small retailers. This would, however, require a new enabling regulation from the Council, and the other proposed amendments should thus not depend upon this, as it may delay the revision procedure.

58. With regard to the other proposals put forward in Option II, reference is made to the discussion above. The EEA/EFTA States support these proposals. Most of the amendments should apply without regard to the parties' market-share, at least as regards the scope of the regulations, i.e. extending them to cover services, goods for processing and agreements between more than two parties.

9.3 Option III

59. It follows from the discussion above that, provided the block exemptions are extended as set out in Option II, a differentiation of the rules is required. In the EEA/EFTA States' view, this can be achieved by the introduction of market-shares. It is important that the market-share limits must be reasonably high in order to reduce legal uncertainty, and that parties exceeding the limit should not loose the benefits of the automatic exemption, but be subject to a more extensive list of conditions or an extended black-list.

9.4 Option IV

60. Option IV entails, as indicated above, interesting opportunities. The development of workable procedural mechanisms that can enable undertakings to establish whether an agreement infringes Article 85(1) or not, seems to be the solution that best complies with both the case-law of the Court of Justice and the findings of economic theory.

61. The EEA/EFTA States would like to stress the importance and usefulness of a further analysis and development of the option. It is not entirely clear whether the option, as presented in the Green Paper, may be implemented within the confines of Article 85(1) and Regulation 17, or whether it requires a new enabling regulation from the Council. A revision of the system and principles of Article 85 should preferably be subject to a broader and more in-depth analysis where also horizontal agreements and specific sectors are included.

* * * * * *