



European Court of Justice on online sales in the context of a selective distribution network

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Summary

On October 13 2011 the European Court of Justice (ECJ) ruled on restrictions on online sales, clarifying that selective distribution agreements imposing a general and absolute ban on the sale of cosmetics and personal care products by selected (authorised) distributors to end-users via the internet might result in contrast with EU competition rules.

The ECJ has followed the Advocate General's opinion on the same lawsuit (see our contribution of March 16 2011 <http://www.lexology.com/library/detail.aspx?g=40e08c79-3bb2-422f-841e-8f1502d5e94c>), according to which in order to comply with EU law, distributors should be free to sell within a selective distribution system, both actively and passively, to all end users, located outside the physical trading area, who wish to purchase the products via the internet.ⁱ

Facts

Pierre Fabre Dermo-Cosmétique SAS ("PFDC") manufactures and markets, mainly through pharmacies, pharmaceutical, homeopathic and para-pharmaceutical products. PFDC's products are distributed through a selective network, where:

- products are sold only through authorized distributors, chosen on the basis of certain criteria (e.g., quality of their sales outlets, qualification of their staff and their commitment to ensuring the physical presence of a qualified pharmacist, felt to be necessary for the dispensing of the products);
- distributors are prevented from selling the products to non-authorised distributors.

PFDC's selective distribution agreements included a clause excluding *de facto* all forms of internet sales, as it required each distributor:

- to sell the concerned products only in a physical space, and
- to supply evidence that a qualified pharmacist will be physically present at its outlet at all times.

On October 29 2008 the French Competition Authority found that PFDC's ban on internet sales for its distributors had infringed national and EU competition rules, namely:

- Article L.420-1 of the French Commercial Code and
- Article 81 of the EC Treaty (now Article 101 of the Treaty on the Functioning of the European Union - TFEU).

PFDC was ordered to remove any provision in its selective distribution agreements that effectively prohibited internet sales of its cosmetics and personal care products. The authority fined PFDC €17,000.

PFDC challenged the Competition Authority's decision before the Paris Court of Appeal, claiming that the purpose of its selective distribution agreements was to ensure a satisfactory level of service for the consumers, thus not to restrict competition.

PFDC also argued that the practice in question was exempted under the Vertical Agreements Block Exemption Regulation (2790/1999)ⁱⁱ (now EU Regulation 330/2010),ⁱⁱⁱ which provides for a block exemption for distribution agreements which fulfil certain criteria.

On October 29 2009 the Paris Court of Appeal asked the ECJ for a preliminary ruling on whether a general and absolute ban on selling products to end-users via the internet, imposed on authorised distributors in the context of a selective distribution network, conflicts with competition rules.

The ECJ's view

The ECJ had to examine PFDC's ban on internet sales in the light of Article 101(1) of the treaty, which prohibits as incompatible with the internal market:

"all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the internal market."

The ECJ interpreted such provision as meaning that, in the context of a selective distribution network, a contractual clause resulting in a ban on the use of the internet for sales of cosmetics and personal care products amounts, in principle, to a restriction of competition by "object" within the meaning of that provision.

In determining whether a contractual clause constitutes a restriction of competition by object, the content of the clause, its objectives and the legal and economic context shall be taken into account. In the ECJ's view, an individual and specific examination is necessary to assess whether such restriction is objectively justified. In this regard, the ECJ admitted that legitimate requirements, such as the maintenance of a specialist trade capable of providing specific services as regards high-quality and high-technology products, may justify systems of selective distribution, and make them compliant with Article 101(1) of the treaty.^{iv}

The ECJ further stated that a ban on internet sales is not covered by the Vertical Agreements Block Exemption Regulation.

The ECJ disagreed with PFDC's assertion that online sales should be classified as sales from an unauthorised virtual establishment, within the meaning of Article 4(c) of the Regulation. Indeed, as clarified by the Advocate General in its conclusions, and held by the Competition Authority, the Internet is not a virtual establishment, but rather a modern means of communicating and marketing goods and services.

Finally, the ECJ considered that an agreement containing a restriction of competition by object can still be individually exempted pursuant to Article 101(3) of the treaty, provided that the requirements for an individual exemption are fulfilled. The ECJ had not sufficient information before it to assess whether the conditions for an individual exemption were met in the case at hand.

Conclusions

In the context of a selective distribution network, restrictions on distributors relating to internet sales are “hardcore restrictions” within the meaning of the Vertical Agreements Block Exemption Regulation, which are likely to be unlawful, and which take the contract outside the block exemption.

Though it now falls to the French court to issue the final judgment on the lawsuit, it is expected that producers will review their distribution agreements, in particular clauses imposing on selective distributors bans on internet sales, similar to those included into PFDC’s agreements. Otherwise, such clauses might be deemed contrary to competition rules, thus null and void.

In the meantime, just few months before the ECJ’s ruling on the PFDC’s case, the 1-year grace period for producers to review their existing vertical agreements and make necessary changes to comply with the new Vertical Agreements Block Exemption Regulation expired on May 31 2011.

ⁱ Opinion of the Advocate General Jan Mazák, March 3 2011.

ⁱⁱ Commission regulation of December 22 1999 “on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices”.

ⁱⁱⁱ Commission regulation of April 20 2010 “on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices”. Regulation 330/2010 entered into force on June 1 2010 and effectively replaced Regulation 2790/1999 which expired on May 31 2010. Regulation 330/2010 is not relevant to the main proceedings at this time.

^{iv} See C-107/82, October 25 1983, *Allgemeine Elektrizitäts-Gesellschaft AEG-Telefunken AG v. Commission of the European Communities*, paragraph 33.