

OVERVIEW

The EU Treaty prohibits anti-competitive agreements and decisions which may affect trade between EU states which have as their object or effect, the restriction or distortion of competition within the EU common market. The effect must be appreciable. Where any restriction is found to be in contravention of this provision, it is automatically void and unenforceable. It can also be subject to fines by the European Commission.

The modernisation regulations which came into force in 2004 radically alters the way EU competition law works. By abolishing the requirement for notification of agreements, the European Commission has required businesses to make and rely on their own assessment

Certain agreements of minor affect are deemed not to appreciably affect competition. Agreements between competitors are not considered to appreciably affect competition, where the aggregate market share held by the parties does not exceed 10%.

The EU Commission accepts that agreements between small and medium sized undertakings rarely appreciably affect trade between member states. Small and medium sized undertakings are those with a turnover below €50 million or total balance sheet of less than €43 million and employ not more than 250 people. They are generally not caught by EU competition law. Although the EU notice in this regard is not legally binding, it is widely used and followed.

Although an agreement may not have an appreciable affect on competition or trade between member states, it may be caught by EU competition law if one or more parallel networks or similar agreements cumulatively result in the closing of potential opportunities to actual or potential competitors.

Even if an agreement is caught by EU competition law, it may be valid if, broadly speaking the overall economic benefits outweigh the negative impact on competition.

The agreement must

- improve production or distribution or promote economic progress while allowing consumers a fair share of these benefits;
- not impose on firms restraints which are not indispensable to the attainment of these benefits;
- not afford such firms the possibility of eliminating competition in respect of substantial part of the products in question.

UK Competition Law

The Competition Act introduced in the UK in 1998 and reformed in 2002, brings UK competition rules more closely in line with European Union competition law. Agreements are prohibited between undertakings which may affect trade in the United Kingdom or which have the object or effect of restricting competition within the United Kingdom or part of it. The agreement must have an appreciable effect on trade within the United Kingdom to be caught.

The UK Competition Authority accept that vertical agreements do not generally give rise to competition concerns, unless one of the parties enjoys market power or an agreement forms part of a wider network of agreements. The Secretary of State has powers under the Competition Act to make Orders providing for the exclusion of vertical agreements. This has been done.

The UK Government has resolved that the UK competition law should be as close as possible to the EU legislation. Since May 2005 the EU vertical agreement blocks exemption applies so as to exempt vertical agreements under both the UK and European Union prohibition.

Vertical Agreements

Both the EU and UK competition law have been recently reformed so that distributorship agreements raise fewer issues of competition law issues than was once the case. Most distributorship agreements will be exempt under EU rules provided the supplier's market share is below 30% and the agreement should not

contain specified excluded restrictions. Likewise at UK level, since 2005 most agreements that do not fix prices are not restricted.

In 2000 the EU Commission adopted a single block exemption for "vertical agreements". Vertical agreements are agreements or practices entered between two or more businesses which operate at different levels in the production or distribution chain and which relate to the conditions under which the parties may purchase, sell or re-sell goods or services. This covers exclusive distributions, exclusive purchasing and franchising as well as selective distributions and agency arrangements.

If the supplier's relevant market share value for the particular product is below 30% the vertical agreement is covered by the block exemption provided the hardcore restrictions and conditions are not breached. The block exemption lasts up to May 2010.

A market share of 30% of the relevant market on the part of the supplier is the test for "market power". Below 30% no "market power" is presumed. Above 30%, there is no presumption of illegality. A business must make an assessment as to whether an agreement is restrictive of competition. There are Guidelines to assist.

Non-Availability of Exemption

The majority of distributorship agreements will fall within the vertical agreements block exemption. However the exemption will not be available in several situations including the following:

- The supplier has a market share of more than 30%;
- Distribution agreement concerned involves two or more parties co-operative at the same level of production and distribution chain;
- The distribution contains "black list" restrictions.

The block exemption contains a "black list" of restrictions. If any are included the exemption will not apply. The restrictions are as follows:

- Price fixing or maintenance - a supplier may impose a minimum retail price or recommended price provided such provisions do not have the effect of a fixed

or minimum re-sale price as a result of pressure from incentives offered by the parties;

- Territorial restrictions – it is permitted to restrict active sales into a territory reserved by the supplier of which another distributor has been granted exclusivity, provided that this restriction does not limit unsolicited sales by the distributor's customers;
- Restrictions in a selective distribution retail system from making active or passive sales to end users are black listed. In a selective distribution system, there must be no restriction as to whom they may sell. There may be restrictions as to location of the business premises. Distributors in a selective distribution system must be allowed to purchase goods from other appointed distributors within the network.

There are further conditions which are not permitted, even where the market share is not exceeded. These include the following:

- Any direct or indirect "non compete" obligation which last indefinitely or exceeds five years. A "non-compete" obligation is one which requires the buyer not to manufacture, purchase or sell competing goods;
- Any direct or indirect obligation preventing the buyer from manufacturing, purchasing, selling or re-selling goods after termination of the agreement;

It is permissible to have restrictions lasting not more than one year post termination which relate to competing goods. This includes any direct obligation to prevent members of the selective distribution system from selling the brands of specified competing suppliers.

The Commission may withdraw the benefit of the block exemption even when the market share threshold is not exceeded where it finds that the agreement has effects which are incompatible with the purpose of the exemption.

Above the 30% market share threshold, exclusive distribution may be permissible. The requirements for admission to selective distribution system must be applied

objectively and without discrimination. Restrictions imposed on distributors must not be excessive in relation to requirements. There are certain products for which selective distribution has been found to be necessary. Luxury goods, technically complex products or products which combine luxury and complexity may justify selective distribution.

This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.

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