

Your World First



E-Commerce Sector Inquiry

Preliminary report published

September 2016

What happened so far?

On 15 September 2016 the European Commission published its 290 page preliminary report on the e-commerce sector inquiry. The inquiry was launched on 6 May 2015 because the Commission was concerned about restrictions on cross-border e-commerce. It forms part of the Commission's Digital Single Market Strategy, which includes three pillars, one of which is improving access to digital goods and services.

Extensive questionnaires were sent to approximately 2,000 manufacturers, retailers, marketplace providers and price comparison tool providers selling or advertising consumer goods active in the following product categories:

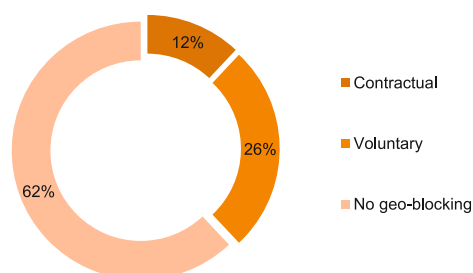
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| — toys and childcare articles | — sports and outdoor equipment | — computer games and software |
| — consumer electronics | — clothing, shoes and accessories | — cosmetic and healthcare products |
| — electrical household appliances | — house and garden | — media |

Regarding digital content, questionnaires were sent to service providers and rights holders of content including film, music, sports and news.

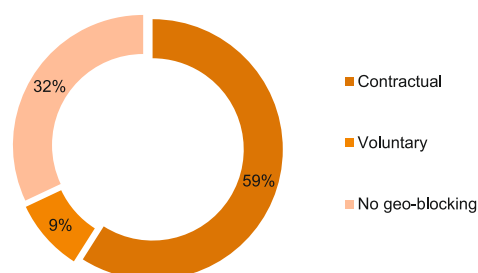
1,800 consulted market players responded to the Commission's questionnaire,
8,000 distribution agreements were analysed, making this the most extensive sector inquiry so far.

Regarding digital content, questionnaires were sent to service providers and rights holders of content including film, music, sports and news.

Of the retailers who sell consumer goods that responded to the questionnaire 38% geo-block:



Of the digital content operators that responded to the questionnaire 68% geo-block:



European Commissioner for Competition, Margrethe Vestager has now confirmed that geo-blocking is one of the main issues in the industry and that the Commission is determined to tackle it.

What did the Commission find?

The Commission has warned that this report should be a reason for companies to review their current distribution contracts and bring them in line with EU competition rules if they are not. According to the Competition Commissioner many companies have already done so during the sector inquiry.

In relation to consumer goods, the following key points can be drawn from the Commission's findings:

- E-commerce has led to **increased price transparency** which has bolstered price competition. That said, the Commission notes increased transparency and **price monitoring activities** may give rise to antitrust issues.
- The use of **selective distribution** systems has increased significantly in the last ten years and the Commission is likely to scrutinise them more closely in the follow-up to the sector inquiry, particularly clauses requiring at least one "bricks-and-mortar" outlet.
- The Commission recognises that **free riding** is a challenge and major concern for businesses.
- The Commission is concerned by the **increase in restrictions and control of manufacturers** over distribution in e-commerce, specifically restrictions on:
 - cross-border sales
 - price comparison tools
 - pricing.
- The Commission expressly states that restrictions on the use of online marketplaces should not be considered a hardcore restriction under the Vertical Block Exemption – which is at odds with the case-law of certain Member States' regulators or courts, for example Germany.
- The Commission considers that some online retailers develop substantial market power.





As regards digital content, the Commission's focus has tended to be on barriers to entry or expansion and innovation – the following are the key points:

- The ability to secure licenses from copyright holders may act as a barrier to entry.
- The Commission is concerned that the way rights are licensed has not adapted to online distribution and may inhibit possible innovation in online transmission.
- Contractual restrictions in licensing agreements on the technology used for transmission, the timing of release and the territory are the norm and may be particularly problematic for new entrants.
- Geo-blocking is widespread in the distribution of online content.
- Long-term licensing agreements and contracts between content providers and rights holders are common and often supported by "soft exclusivity" provisions such as automatic renewal and pre-emption at renewal.
- Payment structures – such as upfront payments – are a further barrier to entry or expansion for new entrants or smaller providers.
- The Commission favours "experimentation", innovation and the provision of the same content on a non-exclusive basis (particularly in payments).
- The Commission also indicates a preference for a move away from the per Member State and/or per right model widely used.

What will the Commission do next?

The preliminary report now opens the public consultation process.

Until **18 November 2016** stakeholders are invited to comment on the preliminary findings. Companies are well advised to do so, in order to ensure that their views are known and that the results of the inquiry will indeed be representative.

The Commission will use the feedback received during the public consultation to fine-tune the preliminary findings for the final report. This final report is due in the first half of 2017.

The preliminary report suggests that the Commission

- Is unlikely to change the competition law framework immediately.
- Is likely to **recalibrate its enforcement priorities**, focusing more on digital business.
- Is likely to **start separate investigations** against individual companies based on the information gathered during the inquiry. The focus will be on:

***Selective
distribution
systems***

***Pricing
restrictions***

***Restrictions
on online
sales***

***Territorial
restrictions***

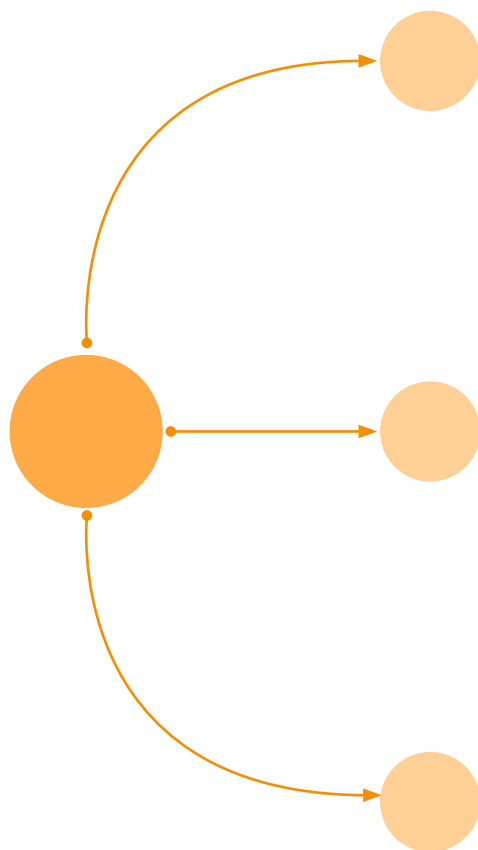
As was the case in past sector inquiries, this may well lead to the Commission imposing fines on some companies.

More generally, the Commission can be expected to **focus more on “vertical restraints”** in its future enforcement policy, an area the Brussels watchdog has mostly left to its national counterparts in the past.

This may lead to a **more level playing field throughout Europe** regarding vertical restraints. Currently each national authority applies its own standards. Companies engaging in cross-border trade bear the costs and complexity of different approaches in Europe and the resulting lack of legal certainty.

Beyond the sector inquiry – The “The Digital Single Market”

The e-commerce sector inquiry is only one element of the Commission’s Digital Agenda. The Commission’s aim is to create what it calls the “Digital Single Market” and the regulator has ambitious plans with far reaching implications for digital business in the EU.



In its **e-commerce package** of June 2016 the Commission published a number of **legislative proposals** aiming at:

- Preventing geo-blocking and generally any discrimination based on nationality or residence
- Making cross-border parcel delivery more affordable
- Increasing enforcement of consumer protection rights in the digital world.

A **package modernising copyright laws** was proposed on 14 September 2016, suggesting inter alia measures to increase portability of online content such as films or music, for example during holidays.

A **VAT simplification package** is expected later in 2016, which would introduce definitive rules for a single European VAT area.

While businesses welcome the idea of removing barriers to cross-border trade not all individual proposals have been well received. Companies fear overregulation and more red tape.

The proposals are currently being discussed and any company engaging in digital business is well advised to closely follow the developments.

How can we help you?

The Commission's findings are preliminary and whilst final conclusions are expected early next year, we do not expect a huge shift in emphasis from the Commission between now and the final report.

Accordingly, companies are "on notice" of the types of issue that the Commission is likely to want to address going forward – either through investigations or a legislative programme.

As a result, all companies involved in e-commerce, whether or not they have directly engaged in the Commission's process, should carefully consider their online practices.

It is particularly important in the context of multi-channel distribution and selective distribution systems and companies should review whether pre-emptive changes are required, including whether agreements currently being negotiated require "change of law" protection in light of future developments in the scope of the Digital Agenda.

The Commission has emphasised that national market structures vary and one-size-fits-all may not be appropriate in all cases – CMS is uniquely placed, with competition lawyers in each major European jurisdiction, to assist you in a broad "house-keeping" exercise, to horizon-spot potential risk areas and provide future-proofed solutions.



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