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The judgment of the Court of Justice in the Coty case changes nothing for the selective distribution model. Discuss.

In *Société Technique Minère*,[1] viewed by many as the first European competition case, the Court of Justice of the European Union ("**CJEU**") considered whether an exclusive distribution agreement would infringe competition law. Since that decision, the law governing agreements between suppliers and distributors has continued to develop, adapting to new challenges presented by the dawning of the technological era.

In this essay, I will explore how the law on selective distribution systems, in which a supplier uses a system of agreements with its distributors to ensure that its products are only distributed by authorised dealers, has developed in recent years, culminating in 2017 in the CJEU's judgment in *Coty Germany v Parfümerie Akzente*.[2] I will set out the current law on selective distribution systems in Section A, discuss the findings of the Court in *Coty* in Section B, and consider the extent to which *Coty* has changed the law on selective distribution systems in Section C. Finally, in Section D I will argue that although *Coty* has not significantly altered this area of law, it cannot be said that *Coty* has changed nothing for the selective distribution model.

A. Selective distribution systems

According to European case law, selective distribution systems based on qualitative criteria may be compatible with competition law, and indeed fall outside the remit of Article 101(1) of the Treaty on the Functioning of the European Union ("**TFEU**") altogether. Selective distribution systems that are based not only on qualitative criteria but also on quantitative criteria will fall within the remit of Article 101(1),[3] but may be justified under Article 101(3) TFEU.

The CJEU has established three criteria in order to assess selective distribution systems which are qualitative in nature, known as the "*Metro* criteria".[4] These criteria are:

a) the goods must be of a type that justifies a selective distribution system;

b) the criteria used to select distributors or retailers are objective and qualitative in nature, and are applied in a uniform and non-discriminatory fashion; and

c) the criteria imposed on distributors do not go beyond what is necessary to protect the quality of the goods.

Several cases have considered the first criterion. In general, complex technological products, luxury branded goods, and products with extremely short shelf-lives may justify a selective distribution system, provided that the other *Metro* criteria are also met.

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1 Case 56/65 *Société Technique Minère v Maschinenbau Ulm*, 30 June 1966

2 Case C-230/16 *Coty Germany GmbH v Parfümerie Akzente GmBH*, 6 December 2017

3 Case C-439/09 *Pierre Fabre Dermo-Cosmetique SAS v President de l'Autorité de la Concurrence*, 13 October 2011

4 Case 26/76 *Metro-SB-Großmärkte GmbH & Co. KG and Verband des SB-Großhandels eV v EC Commission*, 25 October 1977; Case C-31/80 *L'Oreal NV v de Nieuwe AMCK PVBA*, 11 December 1980

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In terms of e-commerce, the main authority on the use of selective distribution systems prior to *Coty* is the CJEU's judgment in *Pierre Fabre v President de l'Autorité de la Concurrence*.[5] In this case, Pierre Fabre had included terms in its contracts with its distributors stating that sales of its cosmetic products had to be made exclusively in a physical space in which a qualified pharmacist was present. This had the effect of excluding distributors from selling the products in question via the internet. The CJEU held that this type of outright ban on internet sales amounted to a restriction of competition under Article 101(1) TFEU.

Pierre Fabre argued that it had used objective criteria applied in a uniform manner in its selective distribution agreements, and that the internet ban was justified by a need to provide individual, face-to-face advice to the customer and by the need to protect the brand's image. The CJEU disagreed, stating that the need to maintain the brand's prestigious image was not a legitimate aim and that, in any event, the ban was disproportionate to achieving any such aim. The judgment states that:

> *"The aim of maintaining a prestigious image is not a legitimate aim for restricting competition and cannot therefore justify a finding that a contractual clause pursuing such an aim does not fall within art.101(1) TFEU"*.[6]

However, it was unclear following *Pierre Fabre* whether the CJEU had meant for the above statement to establish a broader, "illegal per se" approach to selective distribution systems for prestigious products, or whether it only applied to the specific clause at issue in this case.[7] There was therefore some confusion in the years following *Pierre Fabre* about whether selective distribution systems aimed at protecting the prestigious image of a product can ever be compatible with competition law.

B. The *Coty* judgment

The judgment of the CJEU in *Coty* was highly anticipated, as courts and practitioners sought clarification on the lawfulness of internet sales restrictions for luxury products, particularly in light of the *Pierre Fabre* judgment.[8] In this case, luxury perfume supplier Coty Germany had amended its distribution agreement with Parfümerie Akzente so that it contained a clause prohibiting Parfümerie Akzente from distributing Coty products via non-authorised retailers in a discernible manner. This meant that Parfümerie Akzente was now unable to sell Coty products via Amazon.de, as well as other online marketplaces. The Higher Regional Court of Frankfurt made a reference to the CJEU for clarification on whether a ban on the use of online marketplaces for luxury products infringes Article 101(1) TFEU, and whether such a ban constitutes a hardcore restriction under Article 4 of Regulation 330/2010 on the Vertical Agreements Block Exemption ("**VBER**").[9]

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5 *Pierre Fabre*

6 *Pierre Fabre*, paragraph 46

7 *"Internet sales of luxury (and maybe also other) products within selective distribution systems after Coty"*, Prof. Emiliano Marchisio, (2018) European Competition Law Review Vol. 39 8 345-353

8 "*Case C-230/16, Coty: a straightforward issue with major implications"* – Pablo Ibanez Colomo, Chillin'Competition, 16 February 2017

9 Commission Regulation (EU) No 330/2010 of 20 April 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

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In his opinion, Advocate-General Wahl welcomed the reference from the Frankfurt court. He stated that the case provided the CJEU with a much-needed opportunity to clarify the *Pierre Fabre* judgment, noting that *Pierre Fabre* had led to several divergent interpretations by the competition authorities and courts of Member States, stemming from confusion over whether the judgment applied to any selective distribution system with restrictions based on qualitative criteria.[10] He also reiterated a point initially set out in *Metro*, that price competition is not the only form of competition.[11] He stated that, for high-quality and high-technology products:

> *"There are thus legitimate requirements* [...] *which may justify a reduction of price competition in favour of competition relating to factors other than price."*[12]

For the contractual clause at issue in *Coty*, the CJEU found that preservation of a luxury image is a legitimate aim that justifies a restriction of online marketplace sales if the "*aura of luxury*" is necessary to preserve the product's quality. A ban on sales via online marketplaces does not go beyond what is necessary to protect the quality of the product. This is because:

a) the absence of a contractual relationship between the supplier and the online marketplaces means that the supplier is unable to impose the quality conditions on the online marketplaces which it would impose on its authorised retailers;[13]

b) such a ban will not amount to an absolute ban on internet sales;[14] and

c) such a ban will not prevent the distributor from selling Coty products in a non-discernible manner via these marketplaces.[15]

The likely impact of the ban was shown to be minimal; the CJEU quoted figures from the Commission's E-Commerce Sector Inquiry, in which it was shown that, as of 2017, 90% of distributors surveyed still used their own online shops as their main sales channel.[16]

Further, the CJEU held that placing such a restriction on a distributor does not amount to a hardcore restriction under the VBER, where the distributor is still allowed to sell online through its own website and through other authorised retailers. It is not a restriction on the customers to whom distributors may sell, because users of online marketplaces cannot be identified as a particular customer category within the group of online purchasers.[17] It is also not a restriction on passive sales by distributors as it did not prohibit distributors from advertising via the internet and online search engines.[18] It has therefore now been confirmed that, provided that the market share held by each of the undertakings is below 30% as required by the VBER, such

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10 Case C-230/16, *Coty Germany GmbH v Parfümerie Akzente GmBH*, Opinion of Advocate General Wahl, 26 July 2017, paragraph 6

11 *Metro* judgment, paragraph 21

12 *Coty*, Opinion of Advocate General Wahl, paragraph 33

13 *Coty* judgment, paragraph 48

14 *Coty* judgment, paragraph 52

15 *Coty* judgment, paragraph 53

16 Report from the Commission to the Council and the European Parliament: Final report on the E-commerce Sector Inquiry, COM(2017) 229 final, 10 May 2017

17 *Coty* judgment, paragraphs 62-69

18 *Coty* judgment, paragraphs 62-69

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a restriction will not automatically exclude the distribution agreement from the "safe harbour" provided by the block exemption.

C. What role does *Coty* play in the law on selective distribution systems?

The extent to which the CJEU's *Coty* judgment relies on existing case law should not be overlooked. In Figure 1, a flowchart is set out for the current selective distribution model for such cases, demonstrating how *Coty* fits in to this model.

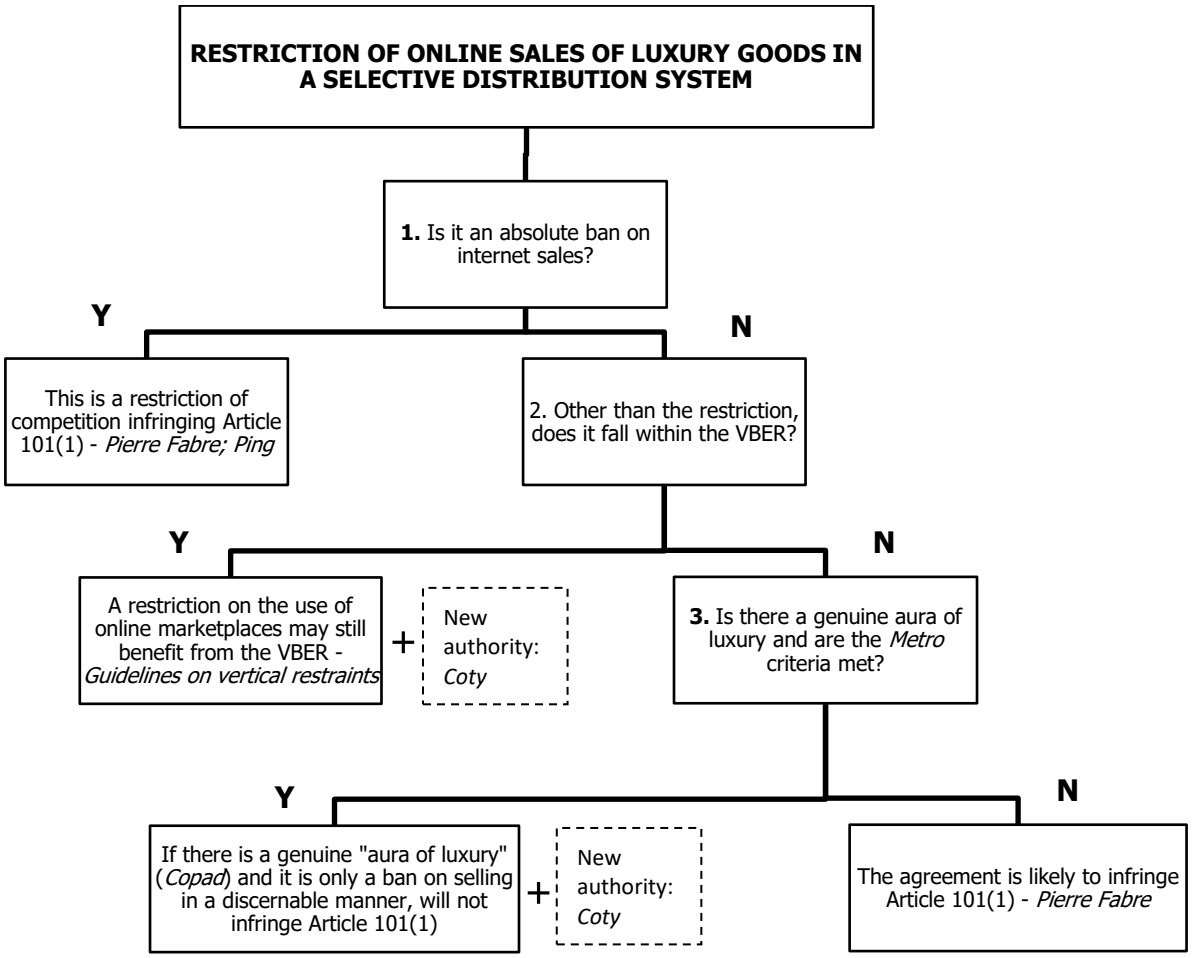

Figure 1: A flowchart showing how the law on selective distribution systems of luxury goods in which online sales are restricted may be analysed.

Internet sales restrictions have previously been considered by the court before *Coty*, most notably in *Pierre Fabre*. However, in *Pierre Fabre*, the ban in question was an absolute ban on internet sales, which was found to be disproportionate and a restriction of competition "by object". This was also confirmed in the recent UK Competition Appeal Tribunal ("**CAT**") judgment in *Ping Europe v CMA*.[19] An absolute sales ban is also a hardcore restriction under the VBER, therefore an agreement containing an absolute sales ban cannot benefit from the block exemption.[20] It is therefore important, when assessing a selective distribution agreement, to ascertain whether or not the contractual clause at issue is an absolute ban on internet sales, or a more limited restriction on internet sales (see Point 1 of Figure 1).

19 *Ping Europe Limited v Competition and Markets Authority*, [2018] CAT 13, 7 September 2018

20 *Pierre Fabre*, paragraphs 51-59

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If it is not an absolute ban on internet sales, the agreement may come within the scope of the VBER (see Point 2 of Figure 1). Paragraph 54 of the Guidelines on Vertical Restraints states that:

> *"*[…] *under the block exemption the supplier may require quality standards for the use of the internet site to resell his goods, just as the supplier may require quality standards for a shop or for selling by catalogue or for advertising and promotion in general. This may be relevant in particular for selective distribution* […] *a supplier may require that its distributors use third party platforms to distribute the contract products only in accordance with the standards and conditions agreed between the supplier and its distributors for the distributors' use of the internet."*[21]

The CJEU followed this point in *Coty*, taking it a step further and confirming that a restriction on online sales via third party platforms was not incompatible with the VBER, where the relevant market share thresholds are satisfied. Nevertheless, where the market share threshold of the parties exceeds 30% of the relevant market, the agreement will fall outside the block exemption, thus failing Point 2 of Figure 1, leaving the agreement open to the risk of infringing Article 101(1).

The *Metro* criteria continue to form the basis for assessing whether a selective distribution system infringes Article 101 (see Point 3 of Figure 1). The *Metro* criteria may be fulfilled if the luxury nature of the goods is important enough to justify the restriction of online sales. This "aura of luxury" point had been discussed prior to *Coty*, most notably in the case of *Copad v Christian Dior and ors*.[22] In *Copad*, the court ruled that the "aura of luxury" that surrounds a luxury product forms an essential contribution to the quality of the product. The CJEU relied on this point in the *Coty* judgment to show that, if the purpose of the restriction of online sales is to preserve a genuine "aura of luxury" and thereby protect the quality of the luxury product, and if the restriction is proportionate and applied in a uniform and non-discriminatory manner, the agreement will meet the *Metro* criteria and will not infringe Article 101(1). If the *Metro* criteria are not met, the agreement is likely to amount to an infringement by object, as was the case in *Pierre Fabre.*

D. Change or clarification?

The purpose of the above diagram is to show that, were *Coty* to be removed, the law on selective distribution systems would be essentially the same. While it is true that *Coty* confirmed the position for luxury goods in the wake of uncertainty left by *Pierre Fabre*¸[23] it did not depart from the existing body of law in a significant manner.

However, although the judgment did not change the law on selective distribution systems in a drastic way, it cannot be said that *Coty* has had no impact whatsoever. Firstly, it confirmed that marketplace bans are not a hardcore restriction under Article 4 VBER. Secondly, by bringing

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21 Commission notice: Guidelines on Vertical Restraints, SEC(2010) 411 final, 10 May 2010

22 Case C-59/08 *Copad SA v Christian Dior couture SA, Vincent Gladel and Société industrielle lingerie (SIL),* 23 April 2009, paragraphs 24-26

23 "*Internet sales of luxury (and maybe also other) products within selective distribution systems after Coty*", Prof. Emiliano Marchisio, (2018) European Competition Law Review 39 8 345-353

together different aspects of previous judgments and guidelines, the CJEU has increased legal certainty surrounding the issues of marketplace bans and the selective distribution model.

In *Coty*, the CJEU explained that *Pierre Fabre* did not seek "*to establish a statement of principle according to which the preservation of a luxury image can no longer be such as to justify a restriction of competition, such as that which stems from the existence of a selective distribution network, in regard to all goods, including in particular luxury goods, and consequently alter the settled case-law of the Court.*" [24]

Although the CJEU distinguishes the facts of *Pierre Fabre* from those in *Coty*, this statement demonstrates that the CJEU was not attempting to depart from the legal conclusions of *Pierre Fabre* in *Coty*. Rather, it confirms that the scope of *Pierre Fabre* is limited to absolute bans of online sales, confirming that the court should assess each selective distribution agreement on a case-by-case basis in order to decide whether restrictions imposed on distributors can be justified in each case.

Many commentators have welcomed this clarification of the law on selective distribution systems.[25] This includes the European Commission, which has stated that the judgment gives *"more clarity and legal certainty to market participants"*.[26] Therefore, although *Coty* does not depart from the pre-existing legal framework, in clarifying previous case law, it makes an important contribution to the law on selective distribution models, particularly with regards to luxury goods.

E. Conclusion

Overall, whilst it could be argued that the *Coty* judgment changes nothing for the selective distribution model, one must acknowledge the utility of clarification of the law, which reduces areas of ambiguity and the potential for misunderstanding. Indeed, it is often that case that when judges are said to be "making" or "changing" the law, they are in fact simply clarifying the existing law. So while it is unlikely to result in a sea-change in the courts' approach to selective distribution models, it cannot be said that it changes nothing; competition authorities and courts will be able to apply the law to future selective distribution agreements with increased certainty, and it will also provide greater certainty for companies. The benefits of the CJEU's clarification of the law in the *Coty* judgment should therefore not be underestimated.

Looking to the future, AG Wahl's opinion in *Coty* suggests that marketplace bans for "*high-quality*", "*high-technology*" and "*high-end*" products are likely to be compatible with Article 101(1) TFEU.[27] However, as the importance of online marketplaces such as Amazon continues to increase, the impact of such bans on consumer access may begin to outweigh the need to protect the "aura of luxury" of high-end products. The courts will have to continue to develop and clarify the law on selective distribution systems in order to keep up with the fast pace of technological change.

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24 *Coty* judgment, paragraph 35

25 *"Where do we stand after Coty?",* Yves Botteman and Daniel Barrio Barrio, Competition Law Journal, 1 October 2018, pages 20-26; "*From Metro To Coty: A Story To Be Continued? The CJEU's Judgment In Coty Germany GmBH V Parfümerie Akzente GmBH",* Andrea Cicala, Kurt Haegeman, Rachel Cuff, Italian Antitrust Review [2017] Volume 4, No. 2

26 European Commission Competition Policy Brief: "*EU competition rules and marketplace bans: Where do we stand after the Coty judgment?"*, April 2018

27 *Coty*, Opinion of Advocate General Wahl, paragraphs 33 and 93