

## SELECTIVE DISTRIBUTION SYSTEMS: CJEU JUDGMENT IN THE COTY CASE

The Court of Justice of the EU (CJEU) has ruled, in its judgment in the *Coty* case, that suppliers of luxury goods can prohibit the members of their selective distribution system (SDS) from making online sales through discernible third party platforms. However, such platform bans will continue to give rise to risks under EU competition law for suppliers of non-luxury products with high market shares and for suppliers of any product for which sales over third party platforms account for a large proportion of internet sales.

### BACKGROUND

The *Coty* case came before the CJEU when the Superior Regional Tribunal of Frankfurt stayed the proceedings in *Coty* Germany's appeal against a finding that it had infringed Article 101 in order to refer questions on the interpretation of Article 101(1) and the Vertical Block Exemption Regulation (VBER). *Coty* Germany, a supplier of luxury cosmetics in Germany, distributed products through members of its SDS. *Parfümerie Akzente*, an authorised distributor under the SDS, sold *Coty*'s products through its 'bricks and mortar' shops, its own online shop and through Amazon's German platform, *amazon.de*. *Coty* revised the terms of its SDS to require authorised distributors to make online sales of its products through an 'electronic shop window' and to prohibit "the recognisable engagement of a third party undertaking which is not an authorised retailer" of *Coty*. In effect, these restrictions prevented authorised distributors from selling *Coty*'s products on platforms carrying a third party's branding such as Amazon and eBay. *Parfümerie Akzente* refused to accept the revisions and *Coty* brought an action to prohibit *Parfümerie Akzente* from selling through *amazon.de*. The court found that *Coty*'s provision infringed Article 101(1) so dismissed the action; *Coty* appealed and the appeal court referred questions on the interpretation of Article 101(1) and the VBER to the CJEU.

The implications of the judgment differ depending on whether the parties' market shares fall above or below the 30% thresholds of the VBER.

### AGREEMENTS FALLING OUTSIDE THE BLOCK EXEMPTION

SDS arrangements between parties with market shares in excess of the VBER thresholds must meet three conditions set out in the CJEU's *Metro* judgment (the "Metro criteria") in order to fall outside the scope of the Article 101(1) prohibition. These are:

#### Key issues

- Is it a breach of EU competition law for a supplier to prevent its distributors from reselling its products over third party online platforms?
- Does it make a difference if the parties' market shares are below the thresholds of the Vertical Block Exemption Regulation?
- Can platform bans still give rise to competition law risks after the *Coty* judgment in some circumstances?

- the criteria used to select distributors must be objective, qualitative, determined uniformly for all and applied in a non-discriminatory fashion. It was accepted that Coty's SDS satisfied this criterion;
- the nature of the product must necessitate a SDS to preserve the product's quality and to ensure its proper use; and
- the terms of the SDS must not go beyond what is necessary to achieve that.

### **Nature of the product: an aura of luxury**

The CJEU referred to its previous *Copad* judgment in determining that the value of a luxury product is not just in its material worth, but also in the "aura of luxury" that is essential to enable consumers to distinguish the product from others. The court therefore reasoned that protection of the aura of luxury is necessary to preserve a product's quality and a SDS with that purpose would fall outside of Article 101(1).

For suppliers that use SDS arrangements falling outside the scope of the VBER to distribute non-luxury products that do not meet the criterion for necessitating an SDS, competition law risks will continue to arise. In its previous judgment in *Pierre Fabre*, the CJEU suggested that such arrangements amount to a restriction of competition by object and are therefore prohibited irrespective of their effects.

For some products, it may be difficult to determine whether they are sufficiently "luxurious" and different competition authorities may take different approaches to this question. For instance, the President of the German competition authority – which has in the past taken enforcement action against suppliers of running shoes that implemented a platform ban – commented that the CJEU's judgment would have only limited effects on its decisional practice, so implying that running shoes are not, in the eyes of the Bundeskartellamt, "genuinely prestigious" products "whose whole point is to convey an aura of luxury". In contrast, a Dutch court ruled in October 2017 (relying on the reasoning of Advocate General Wahl's opinion in the *Coty* case) that Nike's running shoes were sufficiently prestigious to justify a prohibition on distribution over certain third party platforms.

### **Discernible third party platforms**

The CJEU considered that a restriction on sales through discernible third party platforms did not go beyond what was necessary to protect the quality of Coty's products. According to the CJEU, the absence of a contractual relationship meant that Coty would be unable to require compliance with quality conditions from the third party platform as it could from members of its SDS, which would render the SDS ineffective in preserving the quality of the products.

## **AGREEMENTS FALLING WITHIN THE VBER**

The VBER exempts all arrangements between non-competing suppliers and distributors with market shares below 30% (the VBER thresholds), provided they do not contain certain "hard core" restrictions. These include restrictions on the customers to whom the distributor may sell (subject to certain exceptions which were not relevant in this case) and restrictions on authorised distributors in an SDS from making active or passive sales to end users within the territory of the SDS. The CJEU found that a platform ban was not a restriction on customers to whom distributors may sell, as users of third party platforms cannot be identified as a particular customer category within the

### **What is selective distribution?**

In a selective distribution system the supplier undertakes to sell the contract goods or services, either directly or indirectly, only to distributors selected on the basis of specified criteria and these distributors undertake not to sell such goods or services to unauthorised distributors within the territory reserved by the supplier to operate that system.

group of online purchasers. In addition, it was not a restriction on passive sales by authorised retailers as Coty's distribution agreements allowed distributors to advertise via the internet and online search engines, such that users were able to find their online offer.

## NO DE FACTO BAN ON INTERNET SALES

Both the finding of compatibility of platform bans with Article 101(1) and the decision that such a prohibition is not a hard core restriction under the VBER are dependent on the CJEU's finding that the term did not amount to a de facto ban on internet sales. The CJEU had previously found, in its *Pierre Fabre* judgment, that an absolute ban on internet sales does amount to a hard core restriction of competition by object. In *Coty*, the CJEU found that a platform ban was distinguishable from an absolute ban on internet sales, as it only restricts a specific kind of online sale. In this respect, it relied on the conclusions of the Commission's May 2017 report on its e-commerce sector inquiry and, in particular, its finding that "despite the increasing importance of third-party platforms in the marketing of distributors' goods, the main distribution channel, in the context of online distribution, is nevertheless constituted by distributors' own online shops, which are operated by over 90% of the distributors surveyed."

However, that same report also notes that the proportion of all online sales that are made through third party platforms varies greatly between member states. A third party platform prohibition could therefore have the effect of restricting sales to a larger group of customers in some jurisdictions than in others. Consequently, as noted by the Commission in its e-commerce report, platform bans imposed by suppliers of products for which sales over third party platforms account for a large proportion of internet sales could be considered to give rise to antitrust risks even if otherwise compliant with the criteria for SDS arrangements falling outside the VBER and could also lead to withdrawal of the VBER for those arrangements that do fall within its scope. Those risks may become more pronounced in the future as the proportion of online sales made through platforms such as Amazon increases.

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