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Parallel Session

Distribution and the digital world: new challenges to the vertical / horizontal divide

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Ermelinda Spinelli

Freshfields

Nicole Calò-Niiranen

ABB

Alessandro Di Giò

Freshfields

Ilaria Musco

Doctolib

New challenges to the vertical / horizontal divide in the digital world

Alessandro Di Giò – Counsel

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Freshfields Bruckhaus Deringer

Horizontal v. vertical agreements

Basic notions in the standard antitrust conceptual architecture

"....vertical agreements between undertakings operating at different levels of the production or distribution chain are generally less harmful than horizontal agreements between competing undertakings supplying substitutable goods or services. In principle, this is due to the complementary nature of the activities carried out by the parties to a vertical agreement, which generally implies that pro-competitive actions by one party to the agreement will benefit the other party to the agreement and will ultimately benefit consumers. By contrast to horizontal agreements, the parties to a vertical agreement therefore tend to have an incentive to agree on lower prices and higher levels of service, which also benefit consumers. Similarly, a party to a vertical agreement usually has an incentive to oppose actions by the other party that may harm consumers, as such actions will typically also reduce the demand for the goods or services supplied by the first party. Moreover, the complementary nature of the activities of the parties to a vertical agreement in putting goods or services on the market also implies that vertical restraints provide greater scope for efficiencies, for example by optimising manufacturing and distribution processes and services...."

(2022 EC Guidelines on Vertical Restraints, para. 10)

The origins of the distinction

A fairly recent classification

1963 US Supreme Court, *White Motors v. US*

"we need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a pernicious effect on competition"

1980s Chicago School

- Distinction grounded on economic theory
- A tool for judicial efficiency
- A "safe harbour" from the *per se* illegality rule
- *"Horizontal bad, vertical good"* (R. Bork, 1978)

1998 EC's policy recognition of more favourable treatment

"It is generally recognized that vertical restraints are on average less harmful than horizontal competition restraints" (follow-up communication to the Green Paper on Vertical Restraints)

Significant practical implications

A key notion in the concrete life of enforcement and self-assessment of agreements

- **Vertical block exemption regulation** (wider scope than the exemptions under horizontal block exemption regulations, incl. in terms of market shares)
- **Individual assessment**: higher likelihood of "by object" classification (or application of "rule of reason"); different operation of (legal or *de facto*) presumptions or evidentiary burdens; impact on subsequent judicial review
- Potential impact over access (or not) to **leniency** or **commitments**
- Even potential impact on **(merger) filings** in the increasing jurisdictions attaching filing obligations even to agreements / contractual alliances (only of horizontal nature)

Traditional criticism against the distinction

The weakness of the horizontal / vertical divide have been recognised and flagged for decades

- The **post-Chicago** reaction against the risks of underestimating the impact (even at inter-brand level) of vertical restraints
- "**Vertical competition**": competition for shares of profits of the vertical chain (R.L. Steiner, 1991)
- "*Given the consequences of a restraint being labelled horizontal, the focus of antitrust litigation **often shifts from whether or not the restraint is unreasonable to whether the restraint is properly categorized** as horizontal*" (M.L. Lemley and C.R. Leslie, 2007)
- "*The competition assessment of hybrid commercial practices in distribution [...] unveils the **conceptual weakness** of the vertical/horizontal dichotomy and the risks of a formalistic approach in characterizing the restraints. [...] The labels, vertical and horizontal, **do not always correspond to clear presumptions** of anti- or pro-competitive effects and are **subject to manipulation**"* (I. Lianos, 2009)

New challenges for the dichotomy

Online, data and platforms economies contribute to blur the lines between horizontal and vertical

- Globalisation and technologies support distribution disintermediation: increased importance of (online) direct sales and **dual distribution** issues
- Increasing number of instances in which **horizontal / collusion ToHs** are attached to vertical agreements (e.g. **MFN**)
- Disruptive business model of **online marketplaces** (not only hybrid)
- Growing number of cases where the parties **overlap at multiple levels** of the value chain: greater vertical integration; wider markets (?) facilitating overlaps in supply / services relationships, e.g. gathering and processing of **personal data** (or even a **market for online users' attention**)

The response from EU legislation and guidance

*"Undertakings active in the online platform economy play an increasingly important role in the distribution of goods and services. They enable **new ways** of doing business, some of which are **not easy to categorise** using the concepts applied to vertical agreements in the brick-and-mortar environment"*
(2022 EC Guidelines on Vertical Restraints, para. 94)

- Vertical agreements still subject to a **separate legal framework** from horizontal ones
- Despite the increasingly blurred lines, there is arguably room for **improving the «dialogue»** between the two frameworks: currently, few quick references in the VGs to the HGs (hybrid marketplaces; distribution agreement with a competing manufacturer)
- The natural effect is that a (increasingly) large area is **not covered** by either BERs / Guidelines, e.g.: parity clauses other than online retail; marketplaces limitations other than those in the VBER; to some extent, non-reciprocal distribution agreements between competing suppliers (and any restriction within them)
- Is the definition of «**potential competition**» still adequate or sound?

The new VBER / VGs against the challenges

Uneasy task, while attempting to strike a balance between a more prescriptive DMA-style and a flexible approach. Some examples

- Exclusion of VBER / vertical qualification in case of **upstream competition**, regardless of relevance / weight
- In turn, within dual distribution the boundary of legitimate info exchange relies on the concept of "*…necess[ity] to **improve the production or distribution** of the contract goods or services*"

- Radical distinction between **narrow and wide retail parity clauses**, grounded on a mix of vertical (free-riding) and horizontal (competition between platforms) concerns, which however heavily depend on concrete market conditions (see now UK CAT 8/2022 annulment judgement of the CMA MFN decision)

- The exclusion of **hybrid marketplaces** from the VBER: no relevance of the actual degree of competition or market shares for the products involved?
  What about supply relationships (as opposed to marketplaces services)?

A dichotomy fit for the digital age?

- **Is the horizontal / vertical dichotomy still helpful and does it remain the prime antitrust qualification tool for agreements?**
- **Does it still serve (effectively) its original judicial efficiency purpose?**
- **Is there a risk that an «horizontal» qualification becomes a way in (or shortcut to) the «object box» (*i.e.* so as to avoid an effects-based analysis)?**
- **Is it still the best approach to regulate vertical and horizontal agreements separately, under different legal frameworks?**
- **Towards a holistic effect-based analysis? Shift to new or other categories?**

New challenges to the vertical / horizontal divide in the digital world

END

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